NOTES: ODC MEETING - JUNE 1986: Summary of Notes of Eugene H. Rotberg, Vice President & Treasurer, World Bank

<u>MYTH I</u> - IBRD NOT A LEVERAGED INSTITUTION. IT NEEDS INCREASED FINANCIAL RESOURCES IN THE FORM OF A GCI FROM GOVERNMENTS TO INCREASE ITS LENDING.

Not so, if by financial resources we mean budgetary outlays from governments.

a. We do not need government resources to increase IBRD lending-either legally or because of market considerations.

b. Capital need only be "subscribed". It can be all callable, not paid-in.

c. Callable capital may never be called to make loans. It can be called only to make payment of interest or principal to holders of our bonds or our guarantees. Callable capital is, therefore, a contingent liability of all member governments. Calling capital, in effect, would involve the "receivership" of the Bank, i.e., we were unable to meet our obligations from our operational financial position.

d. The Bank has leveraged small amounts of paid in capital to lend and borrow very large amounts at market rates of interest.

e. There should be no confusion about this "callable capital". The concept was incorporated in the Articles of Agreement establishing the Bank in 1946. It was designed for two purposes: first, to

limit the Bank's risk taking to its reserves, paid-in capital and callable capital and second, to assure investors that governments stand behind the Bank. The callable capital has never been called. The Bank's financial operations are conducted with a care and prudence as if there were no callable capital for investors to rely on.

In the 1960's the U.S. callable capital averaged 200% of the Bank debt. Currently, given the markets perception of the Banks great financial strength--it earns over $1 billion a year profit, with remarkable returns on assets and a very strong financial structure--the U.S. callable capital now represents but 22% of its debt. Investors have also come to rely on the callable capital of other Bank members. The Bank, therefore, is not an institution which needs callable capital because of a market perception that it is in financial difficulty. It needs it simply because its "risk assets" (loans and guarantees) must be covered 1:1 by its reserves and capital.

Permit me now to provide some illustrative data about how the Bank leveraged its paid-in capital:

1. Shortly after the Bank was formed, the U.S. paid $635 million in 1947 in the form of "paid in" capital for the purchase of its shares. The U.S. paid in nothing more until 1971 and $750 million since then resulting in total U.S. paid in capital of $1.4 billion.
2. All other governments have paid in only $2.5 billion over the 40 year history of the Bank. The $3.9 billion represents the total payments made

in the form of actual cash released to pay for subscribed shares from all member governments.

3. Since 1968, governments have paid $2.0 billion of the total 3.9 billion paid for their shares. That's all. Our balance sheet, however, now stands at close to $80 billion.

4. Now how have we leveraged that capital to expand the Bank?

   a. Since 1968 loan commitments rose by $115 billion - from $11 billion to $126 billion.

   b. Since 1970 disbursements increased by $66 billion - from $10 billion to $76 billion.

   c. Gross borrowings rose to close to $100 billion.

   d. In 1966, our paid-in capital represented about 40% of our disbursed and outstanding loans. By 1986, paid-in capital represented only 7% of outstanding loans.

   e. In 1966, paid-in capital from governments represented 60% of our debt. By 1986 it represented only 6% of our debt.

   f. Since 1960 through June 1986 our paid in capital has risen by less than 3 fold-from 1.4 billion to $3.9 billion. Our outstanding debt, however, has risen 33 times from $2.1 billion to $67 billion. Our cumulative loan commitments increased by 25 times from 5.2 billion to 126 billion and our cumulative disbursements 19 times from 3.9 billion to 76 billion.

g. In 1960, our paid-in capital of 1.4 billion was equal to about one half of our disbursed and outstanding loans of 2.8 billion. Today it represents about 1/14 of our outstanding loans.

That is what I mean by leveraging capital.

In short, paid in capital has been de minimus and successfully leveraged. We simply need the power to lend under our Articles through an increase in subscribed - primarily callable, capital. We do not need government cash resources.

MYTH II

THE U.S. CAPITAL MARKET HAS SUPPLIED MOST OF THE FUNDS FOR LENDING TO LDC's.

1. The World Bank lending is supported by borrowings in capital markets. But, of $67 billion debt outstanding, the U.S. medium and long-term domestic market has supplied at most $7 billion.
2. Most loans financed are from borrowings in Yen, DM, SWF, and guilders, and to the extent we lend U.S. dollars, it amounts to less than our dollar borrowings from sources and savings outside the U.S. In short, we have not used U.S. savings for development lending. It has been supplied, virtually exclusively, from Western Europe, Japan, oil exporters, and central banks - excluding the Fed.
3. We hold in investments in U.S. government bonds or in banks, twice the dollars borrowed in the U.S. domestic market. The fact is, even our U.S. dollar borrowings have never left the U.S.

4. Over $10 billion worth of contracts have been won by U.S. manufacturers and suppliers of goods and services-financed almost exclusively by savings from other countries.

MYTH III

THE WORLD BANK SLOW DOWN OF GROSS DISBURSEMENTS-ESSENTIALLY FLAT FOR THE LAST THREE YEARS AND PROJECTED NOW AT $4 BILLION LESS FOR THE NEXT THREE YEARS THAN WE PROJECTED PRE BAKER IS DUE TO BUREAUCRACY, RED TAPE, LETHARGY, AN ABSENCE OF GCI, OR ALL OF THE FOREGOING.

No. Not So.

1. Some borrowers have chosen not to borrow. Too much debt. Some are cancelling loans.
2. Some find bilateral loans less costly - particularly if subsidized to facilitate exports of lender.
3. Some are not creditworthy for Bank loans. Now getting IDA credits.
4. Some have no plans for development. We will not lend if there are no development plans.
5. Others cannot supply the local cost component. We should not take over projects where they have no financial commitment and no external sources except ours.
6. Some cannot meet conditions imposed or the structural changes required.

The fact is, it is an easy matter to lend money - quickly, and increase massively net disbursements without development programs. Commercial banks