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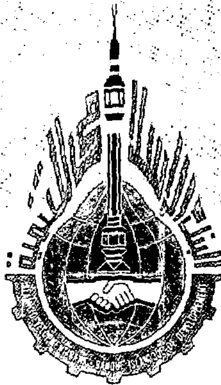

ISLAMIC DEVELOPMENT BANK

RESOURCE CONSTRAINTS IN NANCING ECONOMIC DEVELOPMENT IN IDB MEMBER COUNTRIES

Rajab 1423H (October 2002)

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RESOURCE CONSTRAINTS IN FINANCING ECONOMIC DEVELOPMENT IN IDB MEMBER COUNTRIES

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Rajab 1423H (October 2002)

The views expressed in this paper are entirely those of the authors and do not necessarily represent the views of the Islamic Development Bank Group or its member countries.

PREFACE

Financing development for poverty reduction has become an overcharging objective for the international community, including the major multilateral financial institutions. To the extent that development is constrained by the availability of financial and physical resources, the recent Financing for Development Conference held in Monterrey, Mexico (February 2002) reaffirmed the commitment of the international community to increase official development assistance to mitigate resource constraints faced by many developing countries. A new approach to development based on partnership and policy reform is now underway. To this end, the actions undertaken by developing countries are paramount in determining the process in the fight against poverty. It is postulated that international support for poverty reduction will have only limited impact if governments in developing countries do not commit themselves to well-designed development strategies, sound policies, institutional reforms, and good governance.

Simultaneously, the economies of the IDB member countries are at a crucial juncture in the fight against poverty. Low growth rates exacerbated by low investment levels, weak institutions, and poor governance have caused severe resource constraints that limited the abilities of many IDB member countries to make progress towards the Millenium Development Goals (MDGs). Accelerated progress toward resource mobilization will certainly require action by IDB member countries and support from their development partners and the international financial community. There are by contrast, some LMDCs countries that have implemented sound economic policies, improved their systems of governance, and made some progress toward poverty reduction. The progress made by this group of IDB member countries could certainly be a learning experience for the former group. Meanwhile, the IDB has been deeply involved with its member countries to mitigate the resource constraints through capacity building, financing, technical assistance, and will remain engaged in the period to come.

In recognition of the importance of resource mobilization in promoting poverty-reducing growth, the IDB's Board of Executive Directors suggested that the bank consider preparing an occasional paper on the resource constraints in financing economic development in the IDB member countries. In this context, the paper takes stock of the major resource constraints impeding growth in the IDB member countries with the view of identifying policies that can help alleviate these constraints.

LIST OF ACRONYMS AND ABBREVIATIONS

ADAB	Association of Development Agencies in Bangladesh
ADF	African Development Fund
AEC	African Economic Consortium
AfDB	African Development Bank
AFRACA	African Rural and Agricultural Credit Association
AIDS	Acquired Immuno-Deficiency Syndrome
AMINA	Microfinance Initiative for Africa
ARTAC	African Regional Technical Assistance Centers
ASA	Association for Social Advancement
ATMs	Automatic Teller Machines
BIDS	Bangladesh Institute of Development Studies
BIS	Bank for International Settlements
BOP	Balance of Payments
BOU	Bank of Uganda
BRAC	Bangladesh Rural Advancement Committee
BRI	Bank Rakyat Indonesia
BRI-UD	Unit Desas of Bank Rakyat Indonesia
BUDS	Business Uganda Development Scheme
Caritas	An International NGO
CBF	Capacity Building Facility
CBN	Cost-of-Basic Needs
CBP	Capacity Building Project
CCL	Contingent Credit Lines
CFF	Compensatory Financing Facility
CGAP	Consultative Group to Assist the Poor
CMC	Central bank Musharaka Certificates
CSDP	Cotton Sub-Sector Development Project
CSO	Civil Society Organizations
DAC	Development Assistance Committee
DANIDA	Danish International Development Agency
DFF	Development Finance Fund
DFPF	Distressed Flower Project Fund
DFID	UK Department of International Department
DOD	Disbursed and Outstanding Debt
DSBB	Dissemination Standard Bulletin Board
ECA	Economic Commission for Africa
EFF	Extended Fund Facility
EPF	Export Promotion Fund
ERF	Export Refinance Fund
ESRF	Enhanced Structural Adjustment Facility

EU	European Union
FAO	Food and Agriculture Organization
FATF	Financial Action Task Force
FDI	Foreign Direct Investment
FfD	Financing for Development
FIRST	Financial Sector Reform and Strengthening Initiative
FSAP	Financial Sector Assessment Program
FY01	Fiscal Year 2001
FY02	Fiscal Year 2002
GB	The Grameen Bank
GDDS	General Data Dissemination System
GDI	Gross Domestic Investment
GDP	Gross Domestic Product
GDS	Gross Domestic Savings
GII	Government Investment Issues
GMC	Government Mudharaba Certificate
GNI	Gross National Income
GNS	Gross National Savings
GO	Government Organization
HES	Household Expenditure Surveys
HIPCs	Highly Indebted Poor Countries
HIV	Human Immuno-deficiency Virus
ICD	Islamic Corporate for the Development of Private Sector
IDA	International Development Association
IDB	Islamic Development Bank
IFC	International Finance Corporation
IFIs	Islamic Financial Institutions
IFSB	Islamic Financial Services Board
IIFM	International Islamic Financial market
ILO	International labor Organization
IMF	International Monetary Fund
IT	Information Technology
ITC	International Trade Centers
ITCRF	Investment Term Credit Refinance Fund
LDCs	Least Developing Countries
LDMCs	Least Developed Member Countries
MDF	Multilateral Debt Fund
MDGs	Millennium Development Goals
MENA	Middle East/North Africa
MFI	Microfinance Institution
MFIs	Multilateral Financial Institutions
MF-NGO	Microfinance - Non-governmental Organization
MFO	Microfinance Organization

MIGA	Multilateral Investment Guarantee Agency
MTEF	Medium Term Expenditure Framework
NGOAB	NGO Affairs Bureau
NGOs	Non-Governmental Organizations
NPL	Non Performing Loans
NPV	Net Present Value
ODA	Official Development Assistance
OECD	Organization for Economic Co-operation and Development
PAF	Poverty Action Fund
PAP	Poverty Alleviation Project
PEAP	Poverty Eradication Action Plan
PEM	Public Expenditure Management
PHC	Primary Health Care
PKSF	Palli Karma-Sahayak Foundation
PMA	Plan for Modernization of Agriculture
PRGF	Poverty Reduction Growth Facility
Proshika	A Bangladeshi NGO
PRSP	Poverty Reduction Strategy Paper
PSF	Private Sector Foundation
QIZs	Qualifying Industrial Zones
RDS	Rural Development Sangstha
RFSC	Rural Financial Services Component
RLF	Revolving Loan Fund
RMCs	Regional Member Countries
RMSP	Rural Micro Finance Support Programme
RPE	Rehabilitation of Productive Enterprises Project
SAMIR	Societe Marocaine des Industries du Raffinage
SAPs	Structural Adjustment Programmes
SDR	Special drawing Rights
SHP	Strategic Health Plan
SMEs	Small and Medium Sized Enterprises
SSA	Sub-Saharan Africa
TA	Technical Assistance99
TATF	Technical Assistance Trust Fund
TOT	Terms of Trade
UAE	United Arab Emirates
UEPB	Uganda Export Promotion Board
UGEA	Uganda Grain Exporters Association
UIA	Uganda Investment Authority
UK	United Kingdom
UMA	Uganda Manufacturers Association
UNCCI	Uganda National Chamber of Commerce and Industry
UNDP	United Nations Development Program

UNHCR	United Nations High Commissioner for Refugees
UNICTAD	United Nations Conference on Trade and Development
UNIDO	United Nations Industrial Development Organization
UPE	Universal Primary Education
USA	United States of America
USD	United States Dollar
USH	Uganda Shillings
USSIA	Uganda Small Scale Industries Association
VAT	Value Added tax
WTO	World Trade Organization

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Executive Summary

During the 1990s, the GDP growth rates in the IDB member countries were low and not sufficient to generate incomes required to alleviate the resource constraints experienced by the majority of these countries. These constraints further limit the abilities of the IDB member countries to promote poverty-reducing growth. This is more prominent in many of the Least Developed Member Countries (LDMCs) that were caught in a severe debt overhang problem, thus depleting their already scarce resources. Indeed, the combination of huge debt servicing and inappropriate investment policies triggered an alarming capital flight and created unfavorable conditions to attract foreign capital. The situation was further exacerbated by the current global slowdown in the world economy and the aftermath of September 11 events.

The immediate challenge facing policy makers in these countries is to mobilize domestic resources and seek support from their development partners including major multilateral institutions, regional development banks, and other international organizations in securing foreign resources to finance their resource gaps.

The major focus of this paper is to identify the constraints impeding resource mobilization and, thereby, hampering growth and development in the IDB member countries. The study tracks the performances and progresses of these countries, drawing lessons form good practices and suggesting credible policies and mechanisms that could help the IDB member countries mitigate their resource constraints and make accelerated progress towards achieving the Millenium Development Goals (MDG), of reducing poverty by half by 2015.

The first part of the paper provides assessment of the growth record of the IDB member countries, highlights the resource constraints faced by the IDB member countries, and discusses the broad trends in poverty and growth indicators. Elatedly, successful growth experiences of some LDMCs in Africa are analyzed, identifying good practices and practical lessons as privatization in Mozambique and sound macroeconomic policies in Uganda. Indeed, both Mozambique and Uganda have made significant steps toward achieving many of the MDGs by sustaining growth and reducing poverty in a relatively short period of time.

Following this empirical approach, part two draw lessons from past experiences in linking savings and investment to poverty-reducing growth. Savings rates were found to be relatively low for most member countries during the 1990s, and even negative for others. The low savings rates were mainly a reflection of low

per capita incomes and high propensities to consume. Nonetheless, some LMDCs experienced some improvements in their gross domestic savings rates during the second half of the 1990s, but not enough to sustain their levels of domestic investment. On the other hand, many IDB member countries have maintained, on average investment ratios above 20 percent of GDP. Only two member countries have experienced a savings-to-GDP ratios exceeding 30 percent (Azerbaijan and Malaysia).

To this end, many IDB countries, particularly LMDCs, have experienced huge resource gaps, ranging from around 4 percent to 58 percent of GDP during the 1990s. Consequently, many LMDCs who resorted to both foreign and domestic borrowing to finance the gap became heavily indebted by the end of the 1990s. In addition, more than half of the member countries exhibited, on average, an annual fiscal deficit exceeding 3 percent of GDP. In periods when governments subsidized private consumption, the fiscal deficit crowded out private investment. By contrast, the fiscal deficit crowded in private investment, when governments invested in capital formation, thus confirming previous findings for IDB member countries as in Salih and Diabi, 2001.

The 1990s also witnessed the decline of the share of IDB member countries, as a group, out of the aggregate net resource flows to developing countries, from 28 percent in 1990 to only 8 percent in 1998. Further, private capital flows to IDB member countries also declined significantly in recent years.

Part three of the paper focuses on the factors constraining financial resource mobilization in the IDB member countries .Macroeconomic imbalances, weak institutions, and absence of financial development are characterized as major factors obstructing resource mobilization. Macroeconomic policies and structural adjustments are required to create a healthy environment for investment. The major international financial institutions have made their adjustment lending contingent on macroeconomic stability and stabilization programs (Global Development Finance, 2002).

The paper argues that macroeconomic policies by themselves are inadequate to sustain growth unless supported by a complementary set of structural and institutional reforms. Institutional reforms are needed to put in place a legal framework to ensure that the rule of law is upheld, disputes are settled and contracts are enforced. The paper further argues that the institutional arrangements and the overall legal framework will not be effective if accountability, transparency, and good governance do not characterize them. Hence, the absence of financial reforms and effective institutions is perceived to impede resource mobilization.

Given the social and cultural characteristics of the IDB member countries, the study confirmed that demographic trends over the 1990s, among other economic variables, were the main factors in explaining domestic savings behavior. The data revealed that, the IDB member countries have the highest population growth rate (averaging 2.4 percent), compared to (1.8 percent) in developing countries, while the average GDP growth rate was (3 percent), slightly higher than the population growth rate. The data also show that the low-income IDB member countries have the highest proportion of young dependent (0.88), implying a relatively large number of consumers and relatively few workers. Hence consumption tended to be high relative to earnings, and savings tended to be low. In retrospect, the high dependency ratios tend to constrain resource mobilization.

When the relationship between gross domestic savings and inflation is examined, the data showed that countries with high savings rates (e.g., Bahrain and Malaysia) have low inflation, while those with high inflation (Azerbijan and Kazakhstan) have low savings rates. Consequently, inflation variability could be a constraining factor as it adds to the uncertainties of income and consumption of the poor, thereby reducing their propensity to save. Public policy could be used to influence national savings through the interest rate channel or through the tax policy.

Despite nearly a decade of reforms in many IDB member countries, the financial sectors remain weak and not fully developed. The banking sector continues to dominate as the major conduit for savings and investment and the stock markets are underdeveloped. The few established capital markets lack the proper depth and breadth needed to enhance the efficiency of their operations.

One major characteristic of the IDB member countries financial landscape is the absence of rural finance. The fact that the majority of the poor in the IDB member countries lives and works in the rural areas entails the development of rural financial institutions to provide credit and promote saving. Although conscious efforts were made in some IDB member countries such as Bangladesh and Indonesia, the. need for such institutions in other member countries is crucially urgent, given the successful examples of the Grameen Bank and its replicas worldwide. Other useful lessons can be improved on to augment their impacts on alleviating their resource constraints the detailed country studies discussed in part four of the study.

Part four of the paper focuses on three case studies from different regions of the IDB member countries. In the first case, the experience of the Sudanese Islamic banks in financing agriculture, trade, and small crafts industries is analyzed and documented. The role of the social funds, like Zakat Fund, is also highlighted.

Despite the liquidity problems facing these institutions, the Sudanese experience proved that Islamic finance could play a significant role in alleviating poverty.

The second case study analyzes the role of micro-finance in alleviating poverty in Bangladesh. The Grameen Bank's experience, NGOs and Civil Society Organizations (CSO) as partners in development were discussed. Despite the criticism, micro-finance programs in Bangladesh were able to engage the poor in the development process besides mobilizing their financial resources.

The third case study focuses on the HIPCs debt relief initiative and its role in bridging the resource gap in the Ugandan economy. The program has released much needed resources that were used to fight poverty in Uganda. Uganda is now hailed as the first country to benefit from the program and is headed toward achieving many of the MDGs. Other IDB countries, especially African LMDCs, can emulate the experience of Uganda as the first country to benefit from debt relief.

Other facilitating policies and programs adopted by the multilateral financial institutions and some other international organizations such as the U.N., to help poor countries alleviate resource constraints, are discussed in section five. To achieve the MDGs, the international community has made poverty reduction the central theme of these programs and the analysis of their impacts as the measuring rod to the effectiveness of the development assistance. The IDB member countries can substantially benefit from these programs provided that they adopt and sequence the appropriate policies and meet the specified requirements. For example, microfinance, capacity building and the adoption of technology in development can help greatly in alleviating the resource constraint problem.

In addition, the experience of multilateral financial institutions in financing development lends insightful remarks, useful lessons, and practical policies. Such lessons and policies are summarized in the concluding chapter of the study.

I. BACKGROUND

1.1 Introduction

The growth experience of the last two decades has clearly confirmed the importance of both domestic and external resources in resuming growth in developing countries. In view of the growing concern about sustainable poverty-reducing growth, as emphasized by the United Nations Millennium Declaration, the demand for attracting external resources has increased the competition among developing countries for such resources. Policy makers in these countries, as well as private creditors and multilateral institutions started to think about ways and means to revitalize the situation. Meanwhile, the current global slowdown exacerbated by the bust of the technology bubble at the end of 2000, and the aftermath of September 11 events impacted growth in industrialized countries and consequently, reduced the flow of financial resources to developing countries (IMF Policy Committee Document, 2002). The global slowdown also affected the flow of domestic resources by reducing the revenue generated from the exports of developing countries and limited their access to international capital markets. Indeed, because of inappropriate policies and unfavorable investment climate, poor countries also suffered alarming capital outflows. The consequences were painfully obvious. The failure to reverse capital outflows together with the inability to create favorable conditions to attract foreign capital created severe financial constraints in developing countries.

The IDB member countries as a group are facing the same challenges of promoting growth and reducing poverty. To this end, the economic performance in IDB member countries during the last two decades can at best be described as mixed. In fact, there are considerable variations in actual performance of individual member countries. The countries that implemented sound economic policies and improved their systems of governance have seen acceleration in growth and poverty reduction, and are likely to make significant headway towards achieving the Millennium Development Goals (MDGs). There are, by contrast, other countries where policies have yet to be improved. In fact only a few of the IDB member countries have succeeded in attracting sufficient resources to support their development programs. Despite this limited success, some of them were even unable to sustain such a momentum. On the other hand, the majority of the IDB member countries continue to experience sizeable domestic resource gaps, sometimes exceeding half the size of the GDP. This is a clear indication that the IDB member countries are facing binding constraints in mobilizing both domestic and external resources to finance development.

Notwithstanding the abundant literature on growth and the ensuing issue of resource mobilization, no consensus has yet emerged on what factors lie behind the persistence of these resource constraints in many developing countries, and equally, what policies to adopt for effectively mitigating them.

The debate remains largely centered around the issues of low rates of domestic saving, the inability to attract foreign capital, and the lack of policy effectiveness at the national, regional, and international levels to respond effectively to the challenges of financing for development.

Recognizing the importance of both internal and external resources in promoting growth in its member countries, the IDB organized a Symposium in October 2000, in Beirut, Lebanon on "Resource Mobilization from Capital Markets for Financing Development in IDB Member Countries" (IDB, 2000). The Symposium emphasized the importance of the business-friendly environment that help retain domestic capital, and called for collaborated national efforts to mobilize financial resources, complemented with effective institutions and sound macroeconomic policies. The role of the IDB, as a development institution, in providing support for capacity building and infrastructure development to its member countries, particularly the LDMCs, was emphasized.

The issue of resource mobilization was also addressed at the international level. Multilateral as well as bilateral development agencies continue to play a facilitating role in supporting national efforts to mobilize resources and to generate sustainable poverty-reducing growth. For the most part, these institutions are instrumental in creating an enabling environment through enhancing coherence, and consistency of the international financial and trading systems. In this context, a recent UN Conference on Financing for Development in Monterrey, Mexico recognized the importance of domestic as well as international financial resource mobilization for the common pursuit of growth, poverty alleviation and sustainable development (UN, the Monterrey Consensus, 2002). In particular, the Conference emphasized the need for good governance, sound policies, and institutional development as a prerequisite to achieve these development goals (see Box 1.1).

This study will attempt to take stock of this empirical record and identify the resource constraints impeding growth in IDB member countries, the factors causing them, and the policies and programs that were designed to mitigate them. The overarching objective is, of course, achieving sustainable poverty-reducing growth in IDB member countries.

1.2 Objectives

The paper will attempt to take stock of the major resource constraints impeding growth in the IDB member countries, with a view to identifying policies and operational programs that can help alleviate these constraints. In particular, the paper will focus on the current economic conditions in IDB member countries and the internal and external factors that have limited the mobilization of financial resources. In this respect, the likely impact of the September 11 events on resource mobilization in the IDB member countries will be highlighted. By so doing, the paper intends to propose some policy measures that can help create a conducive and enabling environment to promote poverty-reducing growth in IDB member countries.

Box 1.1:
The UN International Conference on Financing for Development: the Monterrey Consensus

The Conference addressed the challenges of financing for development around the world, particularly in developing countries. The agenda of the Conference covered five major items:

- **Mobilizing domestic financial resources for development**

In the common pursuit of growth, poverty eradication and sustainable development, a critical challenge is to ensure the necessary internal conditions for mobilizing domestic savings, sustaining adequate levels of productive investment and increasing human capacity. Good governance, sound economic policies, a well-developed domestic financial sector, solid democratic institutions and improved infrastructure are the basis for such a strategic objective

- **International trade as an engine for development**

Trade liberalization should ensure that trade plays its full part in promoting economic growth and development for all. International financial institutions, including the regional development banks, should continue to support projects that gradually remove supply-side constraints, improve trade infrastructure, diversify export capacity and support an increase in the technological content of exports, strengthen institutional development and enhance overall productivity and competitiveness.

- **Increasing international financial and technical cooperation for development**

For many countries, Official development assistance (ODA) remains the largest source of external financing and is critical to the achievement of the development goals and targets of the Millennium Declaration. Developed countries are urged to make concrete efforts towards the target of 0.7% of gross

- **External debt**

Sustainable debt financing is an important element for mobilizing resources for public and private investment. External debt relief is critical in liberating resources that can then be directed towards activities consistent with attaining sustainable growth and development. Debt relief arrangements should seek to avoid imposing any unfair burdens on other developing countries and to ensure that resources provided for debt relief do not detract from ODA resources.

- **Addressing systemic issues**

There is an urgent need to enhance coherence, governance, and consistency of the international monetary, financial and trading systems. The multilateral financial institutions, in particular the International Monetary Fund, need to continue to give high priority to the prevention of potential crises and to strengthening the underpinnings of international financial stability.

Overall, the Conference underscored the need to ensure a proper follow-up to the implementation of agreements and commitments, and to continue building bridges between development, finance, and trade organizations and initiatives, within the framework of the holistic agenda of the Conference.

Source: United Nations, 2002

The paper also intends to examine the successful growth experience of some LDMCs, unveiling the sources of this growth, and drawing lessons for other IDB member countries. In addition, the paper will examine, as case studies, three member countries (from different IDB regions) with specific experiences on Islamic financing, micro-financing, small and medium enterprises (SMEs) financing, and the HIPC debt relief initiative. The objective here is to evaluate the effectiveness of such programs in relaxing the resource constraints, and promoting poverty-reducing growth.

Finally, the paper will explore the policies and programs designated by the multilateral development institutions, including the IDB group, to facilitate resource mobilization and alleviate resource constraints in IDB member countries.

1.3 Approach and Data

The paper adopts an empirical approach in reviewing and documenting the growth performance, as well as the initial conditions characterizing the IDB member countries. Meanwhile, The paper will analyze the successful growth experience of selected LDMCs, emphasizing the sources of growth.To this end, the paper uses published and readily available data, reports of the missions mounted to collect unpublished data, and incorporates inside information obtained through discussions with experts in international institutions. The paper will also incorporate the output of the three out-sourced country-studies on three selected LDMCs with a special focus on Islamic financing, micro financing, SMEs, and debt relief programs.

The paper is structured in five main chapters and a conclusion. The remaining Part of Chapter I discusses the link between growth, poverty and resource mobilization. In particular, it highlights the resource constraints faced by the IDB member countries, discusses the broad trends in poverty and growth indicators, and analyzes the successful growth experiences of some LDMCs. Chapter II will attempt to take stock of the recent trends in both domestic and external resources mobilization in the IDB member countries.

Chapter III analyzes the main factors constraining resource mobilization in the IDB member countries. More specifically, it emphasizes the role of governance, sound macroeconomic policy, financial development, and friendly investment climate in promoting poverty-reducing growth. Chapter IV is a case study focusing on the experiences of three LDMCs in alleviating the resource constraints.

Chapter V focuses on the policies and programs adopted by international institutions to mitigate resource constraints and alleviate poverty. In this chapter, some relevant lessons and recommendations on effective ways to mobilize resources are highlighted. Finally, some concluding remarks are given in chapter VI.

1.4 Resource Constraints facing IDB member countries

The overarching objective of achieving the MDGs by 2015 requires action from developing countries and intensified support from the international community. To this end, IDB member countries have to pursue sustained poverty-reducing growth in order to make progress toward meeting the MDGs. However, most of the IDB member countries (especially LDMCs) lack the fundamentals for sustained poverty-reducing growth. All too often, the growth rates required to meet the development objective and the resources needed to finance the implied investment are hampered by many constraints. In these circumstances, identifying

and alleviating the constraints that impede resource mobilization in IDB member countries is an essential first step toward the ultimate goal.

It is important to realize, however, that despite important differences among IDB member countries in terms of size and resource endowments, they share three broad aspects that have an important bearing on the issue of resource mobilization. First, a major part of the population of these countries lives in countries with very low per capita income and underdeveloped production structures (especially LDMC). Second, extremely low levels of human and physical infrastructure inhibit the efficient utilization of the productive resources in these countries. Third, as a consequence of the first two aspects, the economies in these countries, particularly in LMDCs, are highly vulnerable to external shocks arising from fluctuations in the world economy. Certainly, these factors have important financing implications in terms of magnitude and availability of both domestic and external resources.

Indeed, theoretical and empirical literature on growth and development has identified more than 62 statistically significant explanatory variables influencing growth in different countries (ECA, 2000). A part from the initial conditions of real per capita income, life expectancy at birth, primary school enrollment, institutions, political environment and human capital, and financial development are the most critical contributors to development[1]. By and large, many IDB member countries have made significant progress in economic and financial reforms during the 1980s and 1990s. Yet, most of their economies are still inhibited by many structural, institutional, and resource constraints. The extremely low levels of per capita income in LDMCs are, of course, an inherent reflection of these constraints. Hence, the set of constraints that are perceived to be obstacles to resource mobilization, and consequently hampers growth, in the IDB member countries includes (detailed analysis of the deterring effects of these constraints will be given in chapter III below):

(i) *Structural and Macroeconomic Constraints:* Economies in most IDB member countries' are less diversified, small in size, and characterized by inadequate infrastructure. Many countries still depend on primary products, exhibiting a high export concentration, subjecting these economies to export price fluctuations and making them less competitive in the global economy. The inadequacy of infrastructure increases the transaction costs of marketing these products. Further, the underdeveloped structures of these economies, inadequacy of physical infrastructure, and the insufficient stock of human capital have affected the productivity of private capital and impeded the creation of favorable climate for foreign direct investment (FDI).

(ii) *Financial Market Constraints*: Except for a few, financial markets and institutions in the IDB member countries are relatively weak and largely undeveloped in terms of both depth (i.e., volume of financial assets relative to the size of the economy) and diversity of financial institutions and

assets. This weakness has important negative implications on private capital inflows and has certainly hampered the effective mobilization of domestic resources.

(iii) *Debt Overhang Problem*: Many HIPC-IDB member countries did not utilize past external resources usefully. This situation had led to many countries (especially LDMCs) becoming insolvent. Given the strong link between external debt and external resource mobilization, the debt overhang problem in LDMCs implied that a large amount of resources had to be allocated to debt service, thereby reducing the amount of resources available for financing development. The heavy debt burden also created a situation that discourages inflows of new external resources (see, ECA: Financial Sector Reform and Debt management in Africa, Vol. 1).

(iv) *Inaccessibility of International Capital Markets:* The debt problem, inconsistencies in economic policies, high-risk, and the poor financial structure, all have contributed to the creation of binding lending constraints in the international capital markets for most LDMCs. The situation is exacerbated by the external balance conditionality imposed by bilateral and multilateral donors. Consequently, these countries were not able to mobilize sufficient resources or attract significant FDI.

(v) *Institutional and governance Constraints*: Many of the IDB member countries, especially LDMCs, lack the proper market-supporting institutions. Good governance ensures that government actions are transparent, contracts are enforced, property rights are respected, the rule of law is upheld, and the regulatory and economic management agencies are autonomous. The absence of market-supporting institutions and governance had created unfavorable investment climate, inefficiency in public resource management, and non-conducive environment for domestic and foreign investment.

(vi) *Political Instability Constraints:* Political and civil instability, weak institutional capacity and inefficiencies have created unfriendly investment climate, and have had negative implications for resource mobilization in IDB member countries, including disruptive capital flight (ECA, 1999).

1.5 The IDB Member Countries Growth Performance

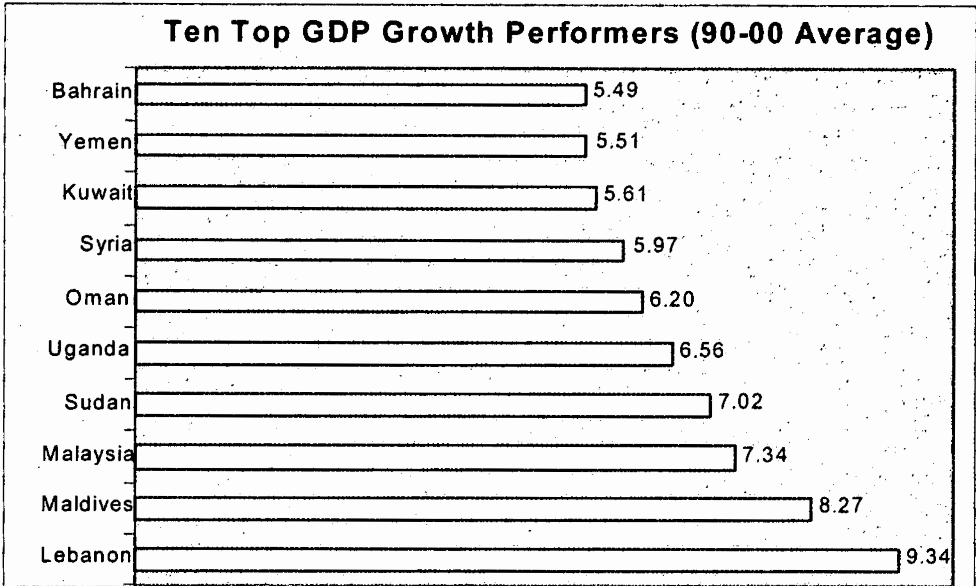
In the last two decades, the IDB member countries showed, at varying degree, more determination toward economic and social development. Over the 1980-1990 period, the average GDP growth rate of the IDB member countries as a whole was 4.4 per cent, surpassing the average growth rates in the developing countries and the world (IDB Monograph, 2001). It is worthy to mention however, that this fast growth can be traced back to the resilient growth record of seven member countries during the said period, namely, Oman, Pakistan, Indonesia, Chad, Malaysia, Turkey, and Egypt. Clearly this growth pace could not be sustained during the 1990s, where the average growth rate was relatively lower (3.0 percent) compared to the developing countries in general, and LDCs in

particular. Most likely, the high negative growth in the CIS member countries during the first half of the 1990s and, to some extent, the setback caused by the 1997 East Asian economic crisis, particularly in Indonesia and Malaysia, are largely behind the fall in growth during the specified period.

The growth experience of individual IDB member countries was relatively unchanged during the 1990s (as can be seen from Table A1.1 in Annex). The number of countries with growth rates of 3 per cent or above increased from 24 in 1990 to 28 in 1995, then dropped to 26 in 1999. Underlying these growth rates, however, are the fluctuation in foreign aid and inadequate production and management systems that have resulted from years of poor economic policies and bad governance. In 1999, only six countries (Albania, Azerbaijan, Guinea-Bissau, Mozambique, Turkey, and Turkmenistan) were able to attain or surpass the 7 percent growth rate (i.e., the threshold deemed necessary to reduce poverty by half in 2015). This suggests that IDB member countries need to redouble their efforts to attain and sustain the required growth rates if they are to improve the standard of living of their people.

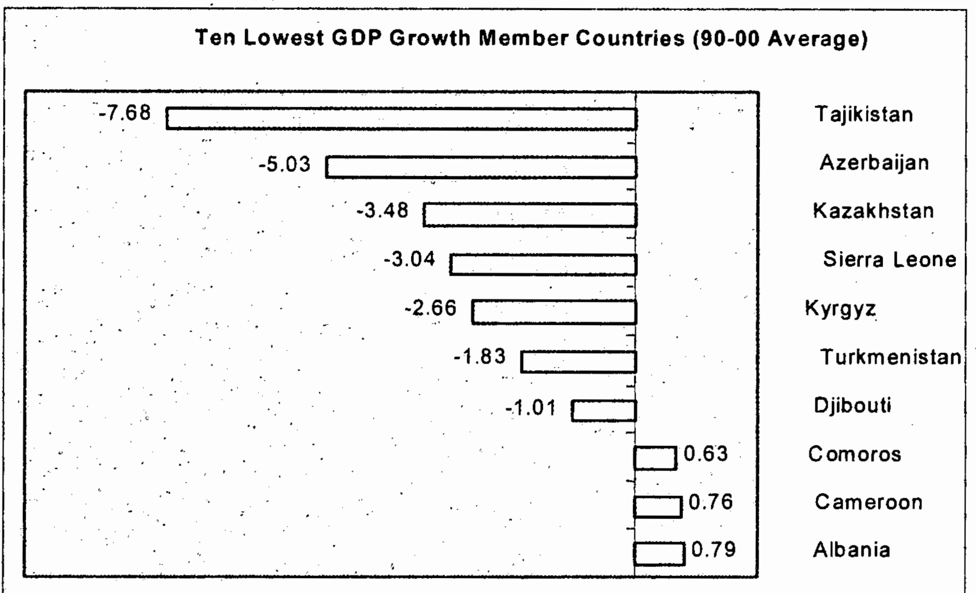
On a regional basis, the average growth in IDB member countries during the 1990s was diverse. For example, in 1999, 16 LDMCs in Africa achieved decent GDP growth rates averaging 3.7 per cent, compared to just 2.2 per cent in 1990. Growth in these countries appears to be converging towards growth rates above the "traditional" African growth rate of 3 per cent, with positive implications for poverty reduction. GDP growth rates averaged 4.3 per cent during the 1990s in the Middle East/North Africa (MENA) region, 5.1 per cent in the South East/South Asia region, 2.6 in Sub-Saharan Africa, and -1.5 per cent in CIS countries (World Bank, Global Economic Prospects, 2002). The ten best growth performers (figure 1.1) averaged 6.7 per cent, while the 10 low performers (figure 1.2) averaged –2.3 per cent. Low income countries like Bangladesh, Benin, Gambia, Guinea and Togo started and finished the decade on the positive side, although their growth rates were modest. Meanwhile, after experiencing double digit growth rates in the early 1990s, some middle income countries like Iran, Lebanon, and Maldives finished the decade with moderate growth rates. The same pattern also applies for Indonesia and Malaysia which were affected by the 1997 Asian crisis.

Figure 1.1



Source: WDI, World Bank, 2002

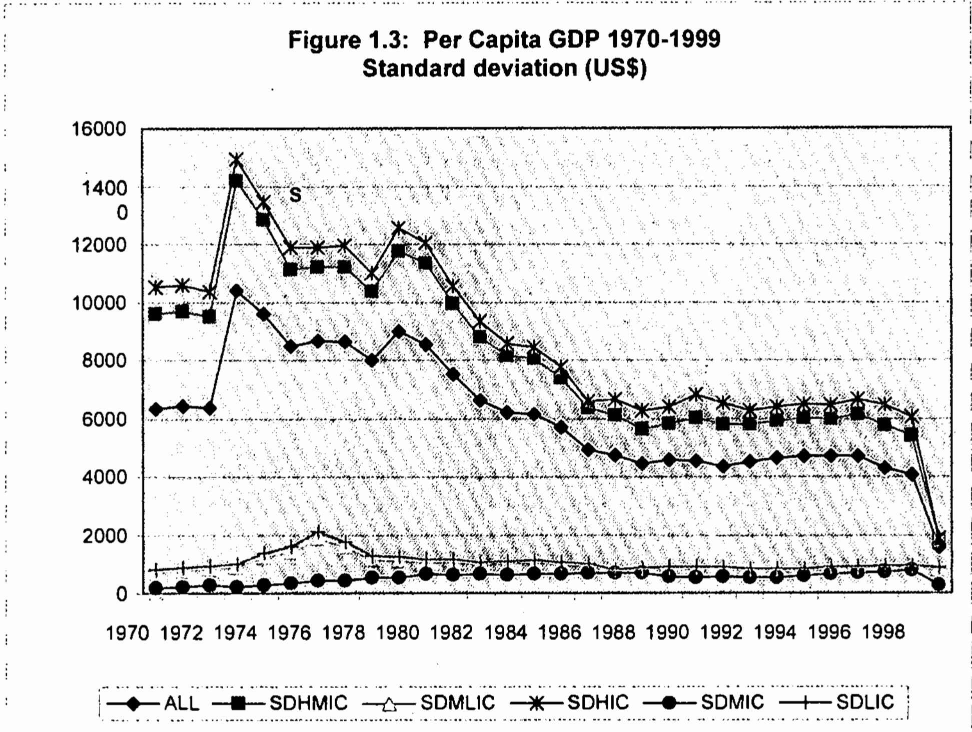
Figure 1.2



Source: WDI, World Bank, 2002

The cross-country disparities in GDP per capita in IDB member countries can be attributed to many factors including, but not restricted to, unequal endowment of natural resources, and human capital, lack of labor and capital mobility, and government policies. To analyze the disparity in the patterns of output

per capita in IDB member countries, we use the concept of convergence, commonly known as "sigma convergence".[2] The time series of this dispersion index for each country classification are depicted in Figure 1.3 for the period 1970-1999.



Source: World Bank, 2001

Some key facts emerge from Figure 1.3. First, the "boom" experienced by the high-income IDB member countries after the oil price surge in 1973 is clearly evident. However, this upward trend was rather short-lived as the dispersion started to follow a downward path during the 1980s before leveling off thereafter. Second, the pattern of dispersion for the IDB member countries is overshadowed by high income countries (SDHIC). After the early diverging trend, disparities between middle income (SDMIC) and low income (SDLIC) member countries begun to narrow during the 1980s and remained largely unchanged during the 1990s. Finally, in 1999, disparities within both high income and middle income countries sharply fell.

The annual GDP per capita growth rates in IDB member countries in the 1990s is shown in Table A1.2 in the Annex,. For the member countries as a group, the per capita income growth remained almost the same, averaging 1 per cent in 1999 and 2.3 per cent in 2000, compared to 0.9 per cent in 1990. However, despite the jump in GDP per capita growth in 2000, the fragile and meager growth

masks wide disparities among individual countries as can be seen from the last two columns of table A1.2. For example, in 2000, just 12 out of 40 IDB member countries experienced negative growth, down from 19 in 1990, 14 in 1995 and 14 in 1999. Meanwhile, only 17 out of 40 member countries experienced a growth exceeding 3 per cent in 2000 compared to 11 in 1990, 14 in 1995 and 17 in 1999.

1.6 Savings, Growth, Income Distribution and Poverty Reduction

Since poverty eradication is now an overarching objective of the international community (U.N. FfD, 2002), decisive actions have to be taken by developing countries and their development partners to reduce poverty by half in 2015. The severity and depth of poverty in IDB member countries is analyzed and documented in Salih (1999), whereby it was reported that more than 660 million people live under poverty. At the root of this alarming situation are low growth, uneven income distribution, and unfavorable external conditions. Indeed, effective mobilization of resources in the IDB member countries appears to be an essential requirement for reducing poverty in these countries. While observed savings rates are also contributing to the low poverty rates, a change in poverty overtime can be attributed to two types of changes: a change due to growth in mean consumption expenditure appropriately adjusted for changes in poverty line; and a change due to the change in the inequality measure (ECA: Economic Report on Africa, 1999). This is important because it links growth to poverty reduction on one hand, and income distribution and poverty reduction on the other.

Using the Gini coefficient to measure inequality in income distribution and the poverty gap to measure poverty[3], Table 1.3 below reflects a fairly high degree of inequality in the distribution of consumption expenditure in a sample of 21 IDB member countries during 1990-2000. The highest degree of inequality is reported for Sierra Leone, with an average Gini coefficient of 62.5 percent, followed by Burkina Faso (55.1 percent), Mali and Niger (50.5 percent), and Gambia (50.2 percent). At the other extreme, the lowest degree of inequality is recorded for Egypt (28.9 percent), followed by Pakistan (31.2 percent) and Indonesia (31.7 percent). The picture of high inequality is confirmed by the poverty-gap ratios, where the highest poverty is reported for Mali (60.5 percent), followed by Niger (54.8 percent), Sierra Leone (51.8 percent), and Burkina Faso (50.9 percent). When the poverty rates are contrasted with average growth rates during the same period, it is apparent that countries with high poverty are experiencing lower GDP growth rates. For example, in Sierra Leone the average growth rate was (-3.0 percent) while 74.5 percent of the population live below US$2 a day, implying a poverty gap of 51.8 percent. On the other hand, countries with high growth rates like Tunisia (5.0 percent) and Turkey (4.1 percent) are characterized with low poverty rates; 2.3 and 5.0 percent respectively. This direct correlation between growth and poverty indicates that there exists a growth rate that is likely to reduce poverty by half in 2015. The question is what growth rate is required to achieve poverty reduction in IDB member countries?

Table 1.1: Poverty Statistics of Selected IDB Member Countries, 1990-2000

HIC	GINI Coefficient	Below $2	Poverty Gap	Squared Gap	Growth Rate	Saving Ratio
Algeria	35.3	15.1	3.6	13	1.6	31.5
Tunisia	41.7	10.0	2.3	5.2	5.0	23.9
Turkey	41.5	18.0	5	24.5	4.1	20.1
MIC						
Indonesia	31.7	55.3	16.5	272.5	4.8	29.8
Jordan	36.4	7.4	1.4	1.9	4.8	3.5
Kazakhstan	35.4	15.3	3.9	15.4	-3.5	17.7
Morocco	39.5	7.5	1.3	1.6	2.6	17.1
Turkmenistan	40.8	59.0	23.3	541.4	-1.8	27.0
LIC						
Azerbaijan	36	9.6	2.3	5.1	-5.0	9.3
Bangladesh	33.6	77.8	31.8	1011.8	5.5	13.8
Burkina Faso	55.1	85.8	50.9	2591.7	4.4	8.6
Egypt	28.9	52.7	13.9	193.2	4.5	14.3
Gambia	50.2	84.0	47.5	2252.5	3.5	4.9
Mali	50.5	90.6	60.5	3663.9	3.4	7.7
Mauritania	37.3	68.7	29.6	878.7	3.5	8.3
Mozambique	39.6	78.4	36.8	1350.9	5.3	-5.1
Niger	50.5	85.3	54.8	3001.3	1.7	2.7
Pakistan	31.2	84.7	35	1227.8	4.0	12.1
Senegal	41.3	67.8	28.2	793.4	3.5	10.1
Sierra Leone	62.9	74.5	51.8	2683.2	-3.0	0.3
Togo	..	..	2.3	5.2	1.4	7.3
Yemen	33.4	45.2	15	223.6	5.5	9.6

Source: WDI, World Bank 2002

Answering the above question is certainly outside the scope of this study. However, a straightforward calculation by the ECA showed that reduction of poverty by half in 17 years requires a decline in poverty at an annual rate of 4 percent. For the North African region (IDB member countries), the study shows that to reduce poverty by half by 2015, GDP growth rates in the range 5-6 percent per year would be required. The required rates of GDP growth for the two poorest regions, West and East Africa (many IDB member countries lie in these two regions) are 7.6 and 8.12 percent respectively.

The relationship between poverty and savings rate is less evident from Table 1.1. Although all countries with high poverty rates experienced low savings-to-GDP ratios; Sierra Leone (0.3 percent), Niger (2.7 percent), Gambia (4.9 percent), and Mali (7.7 percent), there are other countries who experienced both low savings and low poverty (Jordan), and others with low poverty and high savings (Morocco and Tunisia). The notion that the relationship between savings

and poverty requires economic and anthropological factors to characterize seems to hold for IDB member countries.

1.7 Successful Growth Experience in Some LDMCs

Despite the global economic slowdown, which started in the US at the beginning of 2001, output remained strong and growth accelerated in many African countries. Many African countries experienced impressive growth performances during the late 1990s, whereby Africa's overall GDP grew by 4.3 per cent in 2001 from 3.5 per cent in 2000[4]. Some IDB member countries in Africa made significant progress towards realizing the MDGs (Box 1.2). During the second half of the 1990s, Mozambique and Uganda grew by 7.4 per cent and 7 per cent respectively, matching the 7 per cent growth rate deemed necessary for Africa to reduce poverty by half by 2015. Mozambique and Uganda were considered the most successful among African countries in attracting FDI flows in 1999 and have achieved significant reductions in inflation rates and government deficits (as a ratio of GDP) (UNCTAD, 2001).

Many factors contributed to the success of LMDCs including, strong agricultural production, lower oil prices, sound economic management resulting in stronger economic fundamentals, improvement in infrastructures, and higher than expected exports under the U.S. African Growth and Opportunity Act (AGOA). For example, Uganda got a lot of support from multinational and bilateral creditors (see Box 1.2). Uganda was successful in reducing the percentage of people living below the poverty line from 56 per cent in 1992 to 44 per cent in 1996-97 (Chapter IV for more details). It was also able to increase FDI by US$100 million a year since 1995. Another important factor contributing to growth in these countries is the increase in foreign direct investment (FDI). The successful LDMCs showed the prospect of a sustainable growth by removing macroeconomic imbalances, fostering financial sector development and institutional capacity. In this respect, chapter III will provide a detailed analysis of these important factors and their implications on resource mobilization in the context of the IDB member countries.

Box .1.2:
Examples of Progress in Africa

A sample of African countries shows what difference better economic and social policies can make for progressing toward the Millennium Development Goals.

Uganda

- GDP growth averages 6 percent a year in the 1990s
- GDP growth per capita averages 3.3 percent
- Proportion of poor comes down from 56 percent in 1992 to 35 percent in 2000
- Primary enrollment rises from 2.5 million in 1995 to 6.7 million in 2000
- Proportion of nonsalary spending reaching schools more than doubles, from about 40 percent to about 90 percent
- Proportion of children stunted comes down from 51 percent in 1992 to 40 percent in 2000
- Seroprevalance (HIV) rates come down from 30 percent in 1992 to 8.3 percent in 2000

Mozambique

- GDP growth averages nearly 6 percent a year in the 1990s
- Net flows of foreign direct investment shoot up from almost nothing to average about $200 million a year by the end of the 1990s

Mauritania

- Despite a dispersed populace, primary school enrollments reach 90 percent, and school access 93 percent
- Most social indicators up in the past two years

Burkina Faso

- Performance exceeds targets for vaccinations in 2001
- Tuberculosis vaccination rate of 84 percent of infants, against the target of 80 percent
- Measles and yellow fever vaccinations at 65 percent, against the targets of 60 percent

Chad

- Girls' gross primary enrollment rate rises to 58 percent in 2001, up from 31 percent seven years before.

Source: World Bank, 2002.

Box 1.3
How Uganda Achieved Growth and Poverty Reduction

Uganda has been implementing a successful program of reforms since 1997, with strong support from multilateral and bilateral donors. The impact of the combination of government-led reform and development assistance has resulted in a drop in poverty. In 1992 nearly 56 per cent of Ugandans were below the poverty line. By 1996-97 this figure had fallen to 44 per cent. Sound macroeconomic policies produced high growth rates, a steadily improving balance of payments, and a dynamic private sector. From 1994 to 1998 real GDP growth averaged 8 per cent a year; inflation dropped to 5 per cent a year during 1994-97. Although in 1997-98 heavy rains damaged agricultural production and exports, reducing GDP growth to 5.5 per cent, inflation stayed at 5.8 per cent. The government's prudent fiscal and monetary policies, together with a programme of economic liberalization, was so successful that in April 1998 Uganda became the first country to reach its completion point under the Heavily Indebted Poor Countries (HIPC) debt relief initiative. Debt relief through the HIPC initiative is $629 million ($357 million in net present value terms), which will cover about 54per cent of debt servicing to the International Development Association each year for the next 20 years. Debt service relief from all of Uganda's creditors is about $1.3 billion ($660 million in net present value, or about two-fifths of external debt). Including the $65 million in the original HIPC, total debt service relief under the enhanced HIPC initiative will yield roughly $2 billion. By reducing Uganda's debt-service obligations the enhanced debt relief will free resources for poverty reduction.

Uganda is considered a good-practice country because it has promoted good governance by establishing such institutions as the Ministry of Ethics and Integrity, the Auditor General's Office, and the Office of the Inspector General of Government. The government has also designed new regulatory structures for procuring goods and services, and in 1999 it instituted result-oriented management and outcome-oriented budgeting programs to improve service delivery. The combination of good governance, sound economic policies, and effective state regulation of the market process makes Uganda a model case.

Source: IMF 2000a. "Letter of intent."
[http://www.imf.org/external/np/loi/2000/uga/01/index.htm]

Other IDB member countries that had made significant development in the 1990s include the IDB member countries in North Africa and in the CFA zone (Box 1.4). Unlike emerging markets in other regions, those in Africa- Tunisia Egypt, Morocco, South Africa and - were not hurt by September 11 attacks. In fact, between 2000 and 2001 net private flows to these countries nearly doubled, from $4.9 billion to $9.5 billion. In addition, net equity investment jumped from $5.2 billion to $9.3 billion, mainly reflecting large-scale deals in Morocco and South Africa. Net direct equity grew from $3.5 billion to $4.8 billion, driven by privatization in Algeria and Morocco (ECA: Economic Report for Africa 2002). Indeed, the availability of adequate financial resources, whether domestic or foreign, is an essential requirement for financing development. This issue will further be discussed in the next chapter.

Box 1.4:
Progress in the G5, G14, G18, and the Long Term Development in the CFA-zone.

The five good performers in Africa (G5) –Botswana, Mauritius, Morocco*, South Africa and Tunisia*-have demonstrated the their ability to sustain reforms and achieve structural diversification, thus cushioning themselves against possible external shocks. The G5 countries show strong positive trends in the core infrastructure, high and improving educational attainment, international competitiveness, and robust financial markets.

Fourteen potentially emerging Sub-Saharan countries (G14) show the prospect of a sustainable take-off. They made progress in removing macroeconomic imbalances and relative price distortions, including inflation, budget deficit, black market foreign exchange premiums, and real exchange rate misalignment. About half of these potentially emerging countries which belong to the African Financial Community (CFA) zone-Benin*, Burkina Faso*, Gabon*, Mali*, Senegal* and Togo*-are also IDB member countries.

Members of the CFA-zone enjoy currency convertibility, fiscal and monetary policies which are more prudent than Sub Saharan Africa as a whole, and a large amount of financial and technical assistance. These advantages do not appear, however, to have resulted in more rapid economic and human development in the CFA-zone and CFA countries in the Sahel face major structural handicaps.

Currently, a project is under way to understand why CFA-zone performance has been disappointing given the advantages enjoyed by the region, and to devise policy recommendations to improve longer-term development.

The 18 other Sub-Saharan countries, (G18) do not meet the criteria for sustained improvement in economic performance. In addition to the above-mentioned differences with the G14, the G18 have significantly lower investment, less appropriate macroeconomic policies, and greater structural imbalances (related to trade and finance).

Source: Economic Commission for Africa 2000: Transforming Africa's Economies and WIDER, 2002
* IDB member country.

Endnotes of Chapter I

[1] Taking account of the three initial condition variables, recent rigorous robust analysis found only 22 variables to be significant in explaining growth performance among countries. These can be grouped in six broad categories: regional variables, political structure, market distortions, investment share in GDP, production structure, and openness to international trade (see, Sala-i-Martin, 1997).

[2] The sigma convergence is based on time series analysis and focuses on the evolution of a dispersion of a per capita economic indicator. The dispersion index can be measured in several ways. We chose the standard deviation of per capita GDP, as in Barro and Sala-i-Martin (1991, 1992) to assess convergence. According to Barro and Sala-i-Martin (1995), sigma convergence would be observed if the dispersion of real per capita income across a group of countries tends to fall over time.

[3] The Gini coefficient varies from zero (where every person in the society has the same income, indicating the absence of inequality) to unity (where one person gets all the income and the rest receive nothing). The Gini coefficient is frequently expressed in percentages for ease. The poverty-gap ratio, on the other hand, takes into account the extent to which consumption by the poor falls below the poverty line, and the squared poverty-gap ratio measures the severity of poverty.

[4] More specifically, just 16 African countries experienced GDP growth of less than 3per cent, down from 27 countries in 2000. The number of countries with growth rates exceeding 3per cent increased from 26 countries in 2000 to 37 in 2001 (see, Economic Report on Africa 2002).

II. FINANCIAL RESOURCES FOR DEVELOPMENT
THE IDB MEMBER COUNTRIES PROFILE

2.1 Introduction

Availability of adequate financial resources, whether domestic or otherwise, is an essential requirement for every developmental activity of a country. In most developing countries, the domestic resources are limited, inadequate, and insufficient to meet the needs for such developmental needs. Most countries are forced to resort to foreign aid or borrowing at high rates in order to execute their development plans. This scenario has led to two serious problems in international development: aid dependency and high indebtedness.

Since domestic investment is critical for sustaining long-term growth, domestic savings assume a central place in the development strategy of the IDB member countries. Hence, there is an urgent need to adopt policies aimed at creating conditions conducive to boost savings and investment. Yet, high sustainable investment levels would unlikely be financed from domestic savings sources alone. All sources of foreign capital, whether OAD, FDI, private loans from commercial banks, or portfolio investment, have indeed become a necessity for economic development in many developing countries. This is so despite the fact that foreign capital flows are volatile and can create serious economic and financial crisis similar to the Asian Financial Crisis of 1997/98. Moreover, the recent crisis in Argentina and Turkey (2002) illustrates how capital mobility can compound the effects of unsustainable macroeconomic policies and high public sector debt. Moreover, it highlights the challenges facing the international community in assisting countries in crisis (World Bank, Global Development Finance, 2002).

According to the international finance literature, the difference between planned investment and the available domestic savings is the "Financing Gap". Since the resource gap has to be kept within manageable limits in order to maintain macroeconomic stability, donor countries are usually pursued to fill the Financing Gap with foreign aid. Virtually all international institutions addressing the needs of poor countries stress the necessity of both investment and aid for growth in short-run.

However, the international community is doing too little to bridge this gap. By the end of the 1990s, aid to developing countries, whether from the DAC countries or from multilateral institutions (aid here is defined as gross ODA, whether grants or concessional loans) had fallen to almost half the 1991 level (ECA, 2002). Official financing on concessional terms has also been far short of the volume needed to meet the poverty reduction objective. Meanwhile, the resource gap in LDMCs has always been high due to low per capita incomes and high propensities

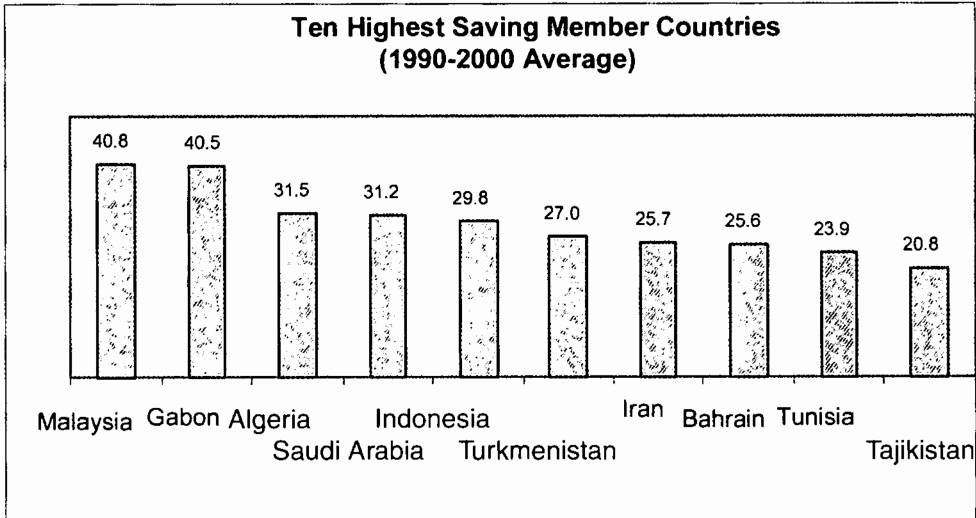
to consume. For many IDB member countries, particularly the LDMCs, the gap was largely financed by borrowing. To adjust to this externality, the IDB member countries, particularly LMDCs, must address the key issue of raising domestic savings. Since domestic resources are crucially important for increasing domestic investment, raising domestic savings must be seen in the broader perspective of increasing incomes. Although significant changes seem to be unrealistic in the short-run, policy makers in LMDCs can make important policy improvements to counteract the effects of externalities and outside shocks. In particular, policy makers should make some adjustments to fluctuations in commodity prices, increased capital flight, decreasing ODA flows, and the debt overhang problem.

2.2 Domestic Saving, Investment and Resource Gaps in IDB Member Countries

Historical savings data in the IDB region reveal that, on average, the ratio of savings to GDP has been on a downward trend, declining from around 34 per cent in 1980 to 24 percent in 1990 and 25 percent in 1999. This is certainly not a very positive sign for the region. However, when the overall picture is disaggregated, it is clear that the primary commodity exporting member countries mainly accounted for this downward shift in the level of the average savings rate. The oil producing member countries (Algeria, Indonesia, Saudi Arabia, Oman, and UAE) as well as others such as Gabon, Bahrain, and Malaysia all had higher savings rates in 1990s (Fig. 2.1). With few exceptions, the savings rates were relatively lower for most member countries in 1990s and even negative for others such as Albania, Chad, Comoros, Djibouti, Lebanon, Mozambique, and Somalia (Fig. 2.2).

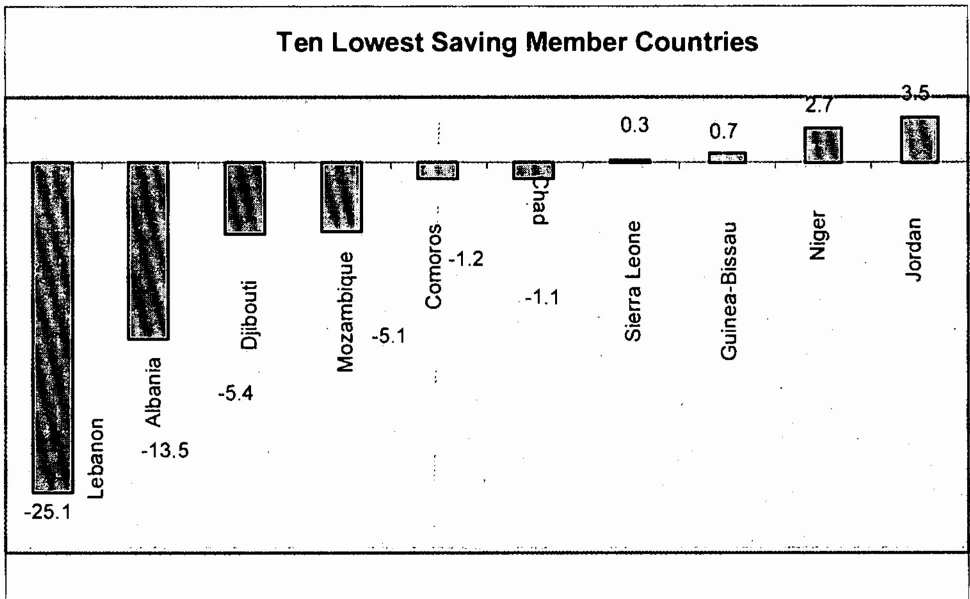
Although many of the LDMCs experienced some improvement in their gross domestic saving rates during the second half of the 1990s, these improvements were not sufficient to sustain the levels of domestic investment (Table 2.1). This partial improvement could be attributed to strong agriculture production, improvement in macroeconomic management, and to high migrant remittances for some member countries (e.g., Bangladesh). Meanwhile, losses by public enterprises, low retained earnings by businesses, and low real rates of interest contributed to the low level of savings in some IDB member countries. Other factors that led to low savings rates in IDB member countries include low incomes, macroeconomic volatility, inefficient financial intermediation and declining tax revenues from foreign trade. The strong reliance on export revenues exposes these countries to externalities arising from supply or price shocks.

Figure 2.1



Source: WDI, World Bank, 2002

Figure 2.2



Source: WDI, World Bank, 2002

To this end, it is worthy to note that the IDB member countries with negative or marginal savings rates were highly dependent on external finance. Indeed, their low savings rates reflect the weaknesses of their financial institutions, and the inefficiencies of their public enterprises. In contrast, high-income member countries, whether resource-based economies or newly industrialized countries, maintained comparatively high domestic savings rates. This relatively better performance can largely be attributed to better fiscal and monetary management, better external sector performance, or both.

Equally, increasing investment is important for productivity growth, because investment can bring more productive technologies and higher skill levels, usually embodied in new plants and equipment. Both private and public investments have to increase in order to exploit the complementarities and synergies important for growth (ECA 2000).

Table 2.1 shows that more than one-third of the IDB member countries has, on average, maintained an investment-GDP ratio above 20 percent throughout the 1990s. These rather moderate rates are largely due to public investments in energy and infrastructure. Only two member countries (Malaysia and Azerbaijan) have managed to increase their investment – GDP ratios to the 30 per cent level. The table also shows that, for the IDB member countries as a group, there seems to be a lack of balance between the savings and investment rates. This implies that the region is not generating enough resources (domestic or foreign) for development purposes, and consequently, there exists an urgent need for significant inflows of external resources.

2.3 Foreign Resource Flows to IDB Member Countries

Unlike their counterparts in Eastern Europe, South East Asia and Latin America, much of the foreign inflows to IDB countries came in the form of ODA, rather than FDI. Yet, for some member countries FDI was the most important source of external finance during the 1990s (Fig.2.3). Comparing the FDI flows (as a ratio of GDP) to IDB member countries with their counterparts in East Asia, Eastern Europe, and Sub-Saharan Africa, it is apparent that the the East Asian countries were able to mobilize more resources better than the IDB member countries. However, the FDI ratio in the IDB countries as a group surpasses the average FDI ratios in Eastern Europe, Sub-Saharan Africa, and the World.

Table 2.1 Domestic saving, Investment and Resource Gap (1990-2000 Averages)

Country	Gross domestic savings (% of GDP)			Gross fixed capital formation (% of GDP)			Resource Gap (% of GDP)		
	90-95	95-00	90-00	90-95	95-00	90-00	90-95	95-00	90-00
Albania	-18.5	-6.8	-13.5	15.2	16.8	15.8	-33.7	-23.6	-29.3
Algeria	30.0	32.4	31.5	27.4	25.5	26.2	2.6	6.9	5.3
Azerbaijan	3.1	11.8	9.3	20.7	29.2	27.8	-17.6	-17.4	-18.5
Bahrain	24.5	26.8	25.6	20.1	13.8	16.9	4.3	13.0	8.6
Bangladesh	12.2	15.3	13.8	17.8	21.2	19.5	-5.6	-5.9	-5.7
Benin	3.0	5.6	4.1	14.7	18.0	16.3	-11.7	-12.4	-12.2
Burkina Faso	7.3	10.1	8.6	21.7	27.6	24.6	-14.5	-17.4	-16.0
Cameroon	19.0	19.1	19.0	15.8	16.6	16.3	3.3	2.5	2.7
Chad	-3.5	1.2	-1.1	8.6	14.1	11.3	-12.1	-12.9	-12.4
Comoros	-1.5	-1.2	-1.2	17.2	12.8	15.0	-18.7	-14.0	-16.1
Djibouti	-8.3	-5.4	-5.4	8.4	10.6	10.6	-16.7	-16.1	-16.1
Egypt	13.6	14.7	14.3	19.5	20.5	20.4	-6.0	-5.8	-6.1
Gabon	40.2	41.9	40.5	22.7	27.8	25.5	17.5	14.1	15.0
Gambia	5.6	2.7	4.9	21.0	18.7	19.8	-15.4	-16.0	-14.9
Guinea	13.8	14.8	14.4	16.9	18.7	17.9	-3.0	-3.9	-3.5
Guinea-	3.2	-2.1	0.7	30.7	19.5	25.4	-27.5	-21.6	-24.7
Indonesia	32.4	27.4	29.8	27.2	26.3	26.6	5.1	1.1	3.2
Iran	26.5	24.3	25.7	21.3	22.6	21.8	5.3	1.7	3.8
Jordan	5.4	2.9	3.5	28.8	24.0	26.1	-23.3	-21.1	-22.6
Kazakhstan	19.7	16.6	17.7	26.9	16.2	20.2	-7.2	0.3	-2.5
Kuwait	2.9	25.8	13.3	19.9	15.0	17.8	-17.0	10.9	-4.5
Kyrgyz	6.3	3.3	4.8	16.9	17.1	16.7	-10.6	-13.8	-11.9
Lebanon	-38.4	-10.7	-25.1	26.6	26.8	25.8	-64.9	-37.4	-51.0
Malaysia	36.5	44.9	40.8	38.1	33.9	35.3	-1.6	10.9	5.5
Maldives	..	47.9	..	37.2	33.0	34.0	..	14.9	..
Mali	6.5	8.9	7.7	23.3	21.9	22.5	-16.8	-12.9	-14.8
Mauritania	8.3	8.4	8.3	19.6	20.4	20.1	-11.3	-12.0	-11.8
Morocco	16.4	17.3	17.1	22.3	21.9	22.1	-5.8	-4.6	-5.0
Mozambique	-13.1	3.4	-5.1	17.1	25.2	21.0	-30.3	-21.8	-26.1
Niger	2.3	2.7	2.7	8.2	9.7	9.1	-5.9	-7.1	-6.4
Pakistan	12.7	11.8	12.1	17.9	15.6	16.7	-5.2	-3.9	-4.6
Qatar	..	35.9	..	27.3	31.9	30.0	..	4.0	..
Saudi Arabia	29.2	33.6	31.2	19.9	18.2	19.0	9.4	15.4	12.2
Senegal	8.5	11.9	10.1	14.3	17.7	16.1	-5.8	-5.8	-6.0
Sierra Leone	4.1	-4.3	0.3	8.2	9.0	8.5	-4.1	-13.3	-8.2
Suriname	21.4	16.4	19.0	17.0	14.3	15.9	4.4	2.1	3.1
Syria	15.0	20.1	17.3	23.5	21.9	22.3	-8.5	-1.8	-5.0
Tajikistan	24.1	17.2	20.8	17.1	16.8	16.6	7.0	0.4	4.2
Togo	8.7	6.5	7.3	16.0	17.5	17.0	-7.2	-11.1	-9.8
Tunisia	24.0	23.4	23.9	28.7	24.8	27.0	-4.8	-1.4	-3.0
Turkey	21.1	19.3	20.1	24.2	24.0	24.1	-3.2	-4.7	-4.0
Turkmenistan	30.5	25.3	27.0	..	41.5	41.5	..	-16.2	-14.5
Uganda	2.4	5.5	3.6	14.9	16.4	15.6	-12.5	-10.9	-12.0
UAE	36.2	..	..	21.8	..	..	14.4	..	..
Yemen	-0.3	18.2	9.6	17.2	22.8	19.9	-17.4	-4.6	-10.3

Source: WDI, World Bank, 2001

Meanwhile, financial inflows to developing countries have declined considerably during the 1990s. In this regard, the share of IDB member countries as a group, out of the aggregate net resource flows to developing countries fell from around 33 percent in 1990 to only 15 percent in 1999[1]. This indicates that the IDB member countries, as a group, have not received enough inflows from foreign sources to finance development. Moreover, when the data is disaggregated on country basis, the majority of them have witnessed a decline in the percentage of both official and non-official financial flows.

Further, the share of the IDB member countries from the aggregate net official capital flows averaged 36 percent during the 1990s, and accounted for 27 percent of the net official flows to developing countries. This share, however, declined significantly from 38 percent in 1990 to around 12 percent in 1997 (Tables A2.1,A2.2, A2.3, and A2.4 in annex).

On the other hand, private capital flows to IDB member countries also declined significantly in recent years despite being unevenly distributed across the member countries[2]. Factors such as lack of consistent reforms, weak financial systems, small market size, human and natural resource constraints, as well as bad governance contributed to the phenomenon. There are prospects, however, for many IDB member countries to enhance private capital inflows provided that measures to attract foreign savings-both public and private-are undertaken.

The IDB member countries did not only suffer from scarcity of foreign capital, but also from improper utilization of invested capital. Inefficient investment has also been a problem for many member countries. In many African IDB member countries with declining per capita growth over the past two decades, the incremental output to capital ratio was lower, on average, than in countries that were experiencing rising growth rates (World Bank, 2000). Increasing productivity and allocative efficiency of foreign capital will enable IDB member countries to generate more resources to overcome their resource constraints and promote poverty-reducing growth.

Given the long-run consequences of borrowing, certain policy measures can be recommended in order to overcome the debt problem. First, proper management of foreign capital resources is essential. Accordingly, member countries should follow proper, well-thought and well-planned policies when importing foreign capital. Second, there should be diversification in the sources of borrowing of a country. It should be less from the institutions asking higher rate of interest or offering tough and difficult conditions. Third, proper deployment of foreign capital is also an important aspect of financial management. The borrowed foreign capital should be used effectively and efficiently to generate industrial production or long-term economic well being of the citizens. Finally, the borrowed money should be utilized exclusively for the purposes specified in the loan agreements. However, priorities have to be taken into consideration.

Figure. 2.3

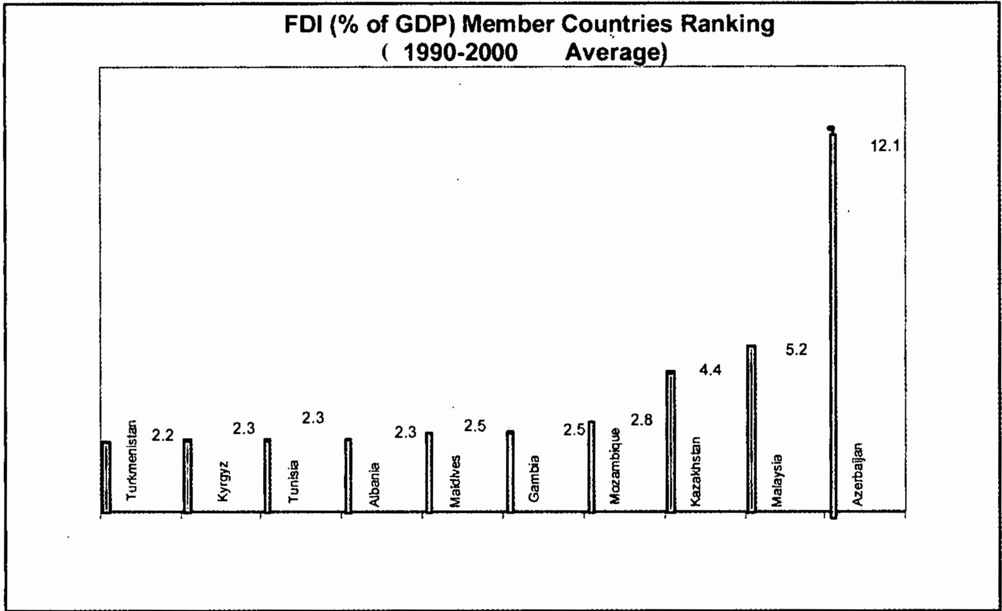
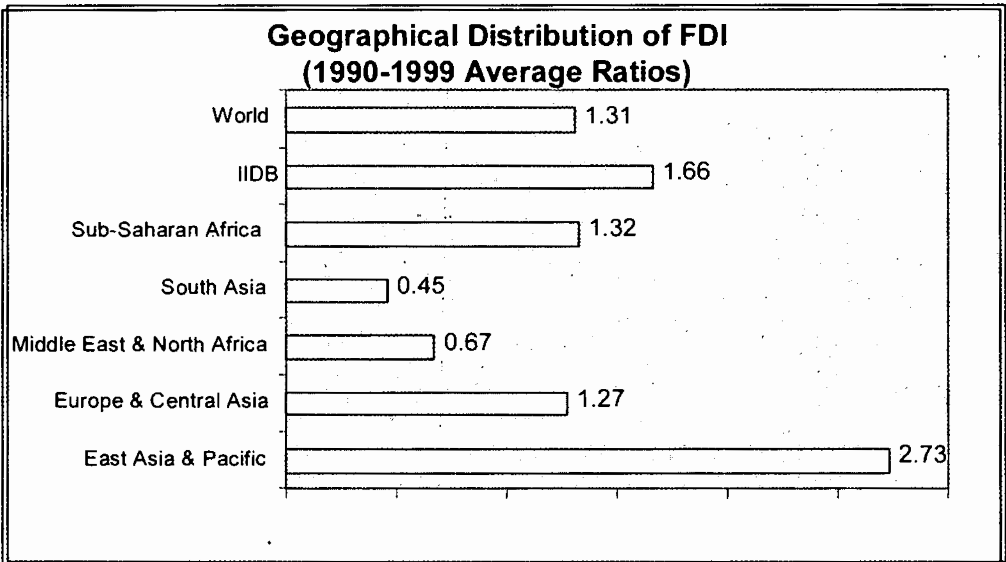


Figure 2.4



Meanwhile, the September 11 events in the US exacerbated the already declining concessional lending was exacerbated by the September 11 events in the U.S. Given the importance of the U.S. economy to the recovery of globally integrated world economy, it was expected that the economic effects of the September 11 events would impact developing countries. Since, the U.S is a major trading partner of many IDB member countries. The impact of the events September 11 is expected to affect the IDB member countries as well. However, since the September 11 events coincided with the global recession, it is not easy to separate their immediate impact on the developing countries in general and the IDB member countries in particular. It is certainly true that many developing countries, including the IDB member countries, have suffered from declining export revenues due to the fall in demand for primary commodities, and from scarcity in foreign capital inflows. A recent study by the OECD (OECD, 2002) argues that, over the long-term, the overall impact of the September 11 events on developing countries could be substantial. The question now is: did the September 11 events impacted resource flows to IDB member countries?

Although the answer to this question is not obvious, it is worthy to note that, in the short term, the global war on terrorism is likely to impact aid as donors attempt to provide economic and humanitarian assistance to countries directly affected by the conflict. In 2002, aid commitments to Afghanistan are estimated to be close to $US2 billion. However, given the limited absorptive capacity of the Afghanistan economy, only $US1 billion is expected to be delivered by the end of 2002. Other IDB member countries, such as Indonesia, Pakistan, and certainly Iraq were also impacted by the events.

Subsequent to the recent events, the US also pledged more than US$1 billion in assistance to Pakistan. Likewise, the Asian Development Bank boosted its financial assistance to Pakistan from US$626 million to US$950million. The World Bank gave Pakistan US$300 million for reforming the banking sector. The IMF also approved a three-year US$1.3 billion loan to Pakistan.

The paper does not intend to dwell upon the impact of the September 11 events. However, the recent developments in the major macroeconomic, financial, and institutional factors in the IDB member countries as well as the emerging global challenges and their impact on resource constraints are explored in chapter III.

Endnotes of Chapter II

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[1] Industrial sources estimate that proposed security measures may increase the *ad valorem* cost of trading internationally by 1 to 3 percentage points. Given that the elasticity of trade flows with respect to transaction costs may be in the -2 to –3 per cent range, this could lead to a significant drop in international trade, negatively affecting openness, productivity and medium-term output growth(Obstfeld and Roggoff, 2001). Thus, the right balance between efficiency and security at the border needs to be found, preferably in agreement with trading partners and on a non-discriminatory basis. There are a number of factors contributed to the reduction of foreign resource inflows. The first was the effects of the East Asian Crisis of 1997/98 and its contagion effects on emerging markets. These crises not only restrained new foreign private sector credit, but also led to withdrawal of previous loans. Second, bilateral credit also contracted because creditors in these countries shifted their support to emerging markets that were impacted by financial instability. Finally, the multilateral institutions have put more emphasis on stabilizing the international financial system by bailing out emerging markets (WDR 1999/2000).

[2] During the boom years, about 90 percent of the private capital flows to IDB member countries were accruing to only five member countries.

III. FACTORS CONSTRAINING FINANCIAL RESOURCES MOBILIZATION IN IDB MEMBER COUNTRIES

3.1 Introduction

The success of any adjustment program aimed at coping with resource constraints for financing development largely depends on maintaining a supportive macroeconomic environment. In the past, a number of IDB member countries initiated well-designed sectoral programs, in areas such as the financial and trade sectors before abandoning or reversing them due to changing economic conditions. Macroeconomic policies are very important and necessary for economic growth, and have spurred good performance across many countries in the world. Major international institutions have made their adjustment lending, to all countries, contingent on macroeconomic unstability and concurrent stabilization program. Hence, financial reforms have become an increasingly important component of adjustment lending. They further tended to have a much higher payoff when macroeconomic imbalances have been brought under control.

It is widely recognized that good macroeconomic and trade policies are necessary but not sufficient to sustain growth. These policies need to be supported by a set of complementary structural and institutional reforms. Institutional reforms are needed to put in place a legal framework to insure that the rule of law is upheld, and that contracts are enforced. However, the institutional arrangements and the overall legal framework will not be effective if accountability, transparency, and good governance do not characterize them. In particular, poor governance and bureaucratic red tape have been major impediments to investment and growth in poor member countries. Indeed, the formulation of pro-poor policies must be matched by equal attention to the required resources, the institutional commitments, and the implementation capacity of the economy. The International Financial Corporation's (IFC) experience with small and medium enterprises (SMEs) programs in some member countries has been disappointing because of the inadequate institutional environment. It is argued that growth has suffered less from a lack of resources than from inefficient investment, mainly because of government ineffectiveness or excessive regulatory burden.

3.2 The Macroeconomic Environment and its Impact on Resource Mobilization in IDB Member Countries

Indeed, a stable macroeconomic environment is critical in promoting saving and investment. Both the IMF and the World Bank continue to emphasize the importance of macroeconomic stability for growth and development financing. In the Poverty Reduction Strategic Paper (PRSP) schemes, the link between poverty reduction and the need for pro-poor policies is clearly emphasized (Box 3.1). For instance, most poverty assessments specifically address the constraints hindering the production abilities of the poor to ensure that the macroeconomic and sectoral policies, including expenditure and tax policies, favor the poor. In particular, factors such as inflation, fiscal deficits, and unemployment can hinder

the ability of the poor in the IDB member countries to accumulate enough wealth to fight poverty. For example, demographic changes are likely to influence private savings by affecting households' income and consumption patterns. Similarly, inefficient public finance can impair the prospects for public savings and possibly crowd out the private sector investment.

Box 3.1

Uganda's PRSP/PEAP: Macroeconomic, Structural and Poverty Linkages

Links between growth and poverty reduction: The PRSP lays out a strategy to promote pro-poor growth by increasing the accumulated assets of the poorest, distributing an equalization grant to the poorest areas, and increasing food production (through agricultural modernization and market access).

Impacts of the taxation system on the poor: On the revenue side, the strategy derives from the recent empirical findings that favor tax reforms, including the introduction of the value-added-tax (VAT), resulting in more progressive taxing system. The PRSP adds that taxes on capital assets used by the poor to be avoided.

Medium-term expenditure framework: The Poverty Action Fund reallocates expenditures to poverty-reducing services, and the budget is being decentralized to districts.

Governance/institutional factors affecting poverty: Measures to increase political accountability are now being considered for funding from HIPC Initiative savings. The PRSP states that transparency will be increased through enhanced flows of information to the public.

Liberalization: The PRSP includes an analysis of the positive impact of the liberalization of the coffee sector, for exemple, on the poor. However, the strategy recognizes that the main beneficiaries of liberalization are cash crop farmers and therefore proposes that more farmers need to enter the cash crop market.

Financial sector reform: The PRSP states that the government is establishing a new regulatory and supervisory structure for microfinance in order to increase poor people's access to financial services. The government has withdrawn from the provision of capital through credit but will still support capacity building.

Privatization: The PRSP states that the government will analyze how to prioritize the privatization of the remaining commercial enterprises and recognizes that red tape and lack of broad participation have adversely affected the privatization process in the past.

Source: IMF, 1998.

3.2.1 Demographic factors and prospects for saving

The notion that demographic factors influence saving rates has been addressed extensively and debated in the literature. In the life cycle model, the age composition of the population is postulated to have a significant influence on the household saving behavior. While the youth and the elderly have low incomes and low savings, those in the middle-age group have higher productivity and incomes. The latter group usually saves more to repay past obligations, pay for their children education, and/or to refinance their retirement. Aggregate savings will, therefore, be affected by the age distribution of the population (Elbadawi and Mwega, 1998).

Examining demographic trends over the 1990s reveal certain characteristics about the domestic saving behavior in the IDB member countries. For example, in 1999, IDB member countries accounted for nearly a quarter of the world population, whereas half of their population lives in three Asian countries: Bangladesh, Indonesia, and Pakistan. The trends also indicate that the IDB member countries have the highest population growth rate (2.4 per cent) compared to developing countries (1.8 per cent). It is worthy to note that the average GDP growth rate during the 1990s (3.0 per cent) was slightly higher than the population growth rate in these countries.

It is apparent from Table 3.1 that during the 1990s, the low-income IDB member countries have the highest proportion of young dependents (0.88). This high age dependency ratio reveals that the population consists of a relatively large number of consumers and relatively few savers. Hence, consumption will be high relative to earnings, and the saving activity will be low. In contrast, the dependency ratio for the high-income member countries is, on average, comparatively low (0.66), albeit relatively high in comparison with the world's high-income group ratio of 0.5. The dependency ratio of the middle income group lies somewhere in between (0.77), compared to the world middle income group ratio of 0.50. Meanwhile, the computed cross-country correlation coefficient between gross domestic saving and age dependency ratio is -0.34.

These demographic factors present numerous challenges for financing development. Certainly, they have some implications on the labor force, savings, the need for health care, education, housing, and other social needs such as the provision of social safety net. The cross correlation coefficient between population growth rate and the gross domestic saving rate is positive, however very small in magnitude. By contrast, when using the rural population proportion or its growth rate, the negative and strong link becomes more evident (-0.72). This may suggest that, as long as a large portion of the population lives and works in the rural areas, savings in the IDB member countries are likely to be low.

Notwithstanding the growing urban population in the IDB member countries, the proportion of the rural population still remains dominant in both low and middle income member countries (66 and 52 percent on average, respectively). Most of the poor population is to be found mainly in rural areas, particularly in LDMCs. In this context, more attention has to be directed towards rural development, with the view to finding effective ways to promote rural savings. Perhaps a system of financial intermediaries at the grass roots would help mobilize the dormant savings held away from the financial system. Setting up (interest-free) banking facilities and financial outlets will have a significant impact on savings mobilization. Equally, developing a good rural infrastructure could be a further impetus to the accumulation of savings among the rural population, particularly in the poor member countries. Civil Society Organization (CSO) and NGOs can play an important role in mobilizing and pooling the resources of the rural population.

Table 3.1 Demographic Changes and Saving Performance in IDB Member Countries (1990-1999 Averages)

Country	Gross Dom. Saving Ratio	GDP Growth Rates	Population Growth Rates	Rural Population Proportion	Rural Population Growth	Urban Population Growth	Age Dependency
Algeria	30.2	1.3	2.05	43.9	0.2	..	0.76
Bahrain	37.2	3.9	3.10	10.1	-1.6	..	0.52
Gabon	41.7	2.8	2.62	..	..	4.5	0.79
Iran	26.7	4.8	1.68	..	..	..	0.83
Kuwait	10.8	10	-0.62	..	..	-0.4	0.63
Malaysia	40.6	7.2	2.63	46.7	..	4.0	0.66
Saudi Arabia	29.8	2.8	2.64	..	..	..	0.79
Tunisia	23.9	5.1	2.89	..	..	..	0.66
Turkey	20.4	3.8	3.09	32.0	-2.8	..	0.58
UAE	36.2	3.8	2.32	..	..	5.7	0.46
MIC							
Indonesia	32.3	4.8	1.68	64.8	..	4.6	0.61
Jordan	4.6	4.9	4.39	..	..	5.3	0.85
Kazakhstan	18.2	-5.3	-0.85	43.4	-0.8	..	0.57
Lebanon	-31.1	11.5	1.81	..	..	2.5	0.65
Morocco	17.1	2.6	2.09	48.3	0.2	..	0.66
Syrian	16.3	6.1	2.92	..	..	3.7	0.92
Turkmenistan	18.6	-3.9	5.01	..	..	2.8	0.76
LIC							
Albania	-14.4	0.4	0.44	..	..	..	0.60
Azerbaijan	12	-7.4	1.19	..	..	1.7	0.60
Bangladesh	13.4	4.9	1.66	..	..	4.1	0.85
Benin	4	4.5	2.86	62.0	1.6	..	1.02
Burkina Faso	8.5	3.8	2.37	..	1.8	..	1.00
Cameroon	19	0.4	2.75	55.8	..	4.7	0.92
Chad	-1.4	2.1	2.86	..	..	..	1.12
Comoros	-3.7	0.1	2.57	69.8	1.8	..	0.96
Djibouti	-10.5	-2.1	2.74	..	..	..	0.80
Egypt	13.4	4.5	2.01	55.5	1.8	..	0.73
Gambia	4.9	3.3	3.54	71.3	2.6	..	0.81
Guinea	14.2	4	2.61	..	..	5.1	0.95
Guinea-	1.2	1.2	2.15	..	1.7	..	0.87
Kyrgyz	4.8	-3.4	1.17	64.7	1.8	..	0.73
Maldives	25.2	7.7	2.53	..	..	..	0.95
Mali	7.7	3.2	2.77	73.5	1.7	..	1.02
Mozambique	-6.6	5.6	3.37	..	..	6.4	0.97
Niger	2.7	1.9	3.98	82.0	2.9	..	1.03
Oman	28.2	6.2	2.47	..	..	7.3	0.92
Pakistan	12.1	4	1.96	..	1.7	..	0.85
Senegal	10.1	3.3	2.54	56.6	1.4	..	0.92
Sierra Leone	1.8	-4.1	..	..	..	4.4	0.93
Suriname	21.3	3.1	1.86	30.4	-2.5	..	0.63
Tajikistan	15.1	1.6	1.72	..	2.5	..	0.86
Togo	7.3	1.7	1.59	69.4	..	4.5	0.96
Uganda	3.8	6.9	3.99	87.6	2.8	..	1.04
Yemen	7.2	3.1	2.93	76.4	3.9	..	1.10

Source: WDI, World Bank, 2002.

3.2.2 Public finance and domestic resource mobilization

Earlier research on economic policy (e.g., Brainard 1967) suggests that public policy alone should be used to influence the national saving level. According to this view, the most direct way to raise national savings is through higher public savings since it is under direct government control. When public savings are not sufficient to finance public investment, the financing gap is to be bridged by non-inflationary sources in order to avoid the crowding-out effects. Such non-inflationary measures usually include social security funds, and the excess liquidity in the banking sector. Governments can also raise extra funds from privatizing state-owned enterprises, from reordering budgetary items according to priorities, and from strict public expenditure management. Public policy can also be used to influence national savings through the interest rate channel. If the government is financing its deficit through bond issue, then the interest rate plays a crucial role in determining the savings and investment levels. For example, in periods of higher inflation, governments have to raise nominal interest rates to offset the effects of inflation. Consequently, higher real interest rates may raise national savings in the short run, but may crowd out private investment in the medium to long-run.

Public policy can also influence national savings through the tax policy. To finance its public expenditure, the government usually adjusts its tax rate to maximize the tax revenues[1]. Table 3.2 shows that, in almost all member countries, government current revenue is not sufficiently high. Except for Kuwait, government revenues in IDB member countries were less than one-third of GDP in 1999. The main sources of government revenue in these countries are taxes on income, profits, capital gains and import duties.

The ratio of tax revenue to GDP indicates the ability and the willingness of the governments in IDB member countries to tax. These ratios range, on average, between 20 percent (Jordan and Malaysia) to 1.1 percent (UAE) during the 1990-1999 period, indicating that the abilities of the tax systems vary widely across IDB member countries. Most of government revenues were generated from non-tax sources, especially for oil producing countries such as Bahrain, Kuwait, Oman, and UAE. Table 3.2 reveals a low taxable capacity in the majority of the IDB member countries. In order to mobilize more resources through taxation, many countries have to reform their tax system, enhancing its capacity and raising its efficiency. IDB member countries may need to broaden their tax bases to counter balance any loss of revenue, but to avoid raising the taxes to unnecessary levels. In particular, taxes on foreign trade may be reduced to facilitate integration in the world trading system. More specifically, the required tax revenue will have to be achieved though tax rationalization, improved tax administration and a broadening of the tax base. Tax reforms would generate revenue and improve macroeconomic management through automatic stabilization:

Table 3.2 Saving, Fiscal Balance and Financing (1990-1999 Averages)

Country	Gross Dom. Saving Ratio	GDP Growth Rates	Fiscal Balance	Financing Abroad	Domestic Financing	Government Expenditures % of GDP	Tax Revenue% of GDP	Non Tax Revenue % of Revenue	Highest Corporate Tax Rate
HIC									
Algeria	30.2	1.3	-1.3	7.4	-6.56	16.7	..	7.2	..
Bahrain	37.2	3.9	-4.5	..	3.39	23.0	..	70.2	0
Gabon	41.7	2.8	0.8	1.3	..	14.5	17.2	30.7	40
Iran	26.7	4.8	-1.1	0.0	1.10	12.7	..	55.7	33
Kuwait	10.8	10	-6.7	..	..	38.6	1.3	96.4	3
Malaysia	40.6	7.2	1.1	-1.16	4.38	12.1	19.8	23.7	28
Saudi Arabia	29.8	2.8	..	..	..	29.8	..	..	45
Tunisia	23.9	5.1	-3.2	1.7	..	16.1	..	16.4	..
Turkey	20.4	3.8	-6.6	-0.5	..	12.3	..	17.7	27.5
UAE	36.2	3.8	0	0.0	..	17.0	1.1	55.8	20
MIC									
Indonesia	32.3	4.8	0.1	0.6	-0.73	7.7	15.8	10.3	30
Jordan	4.6	4.9	-1	1.16	-0.14	23.8	19.7	27.0	..
Kazakhstan	18.2	-5.3	-4	2.8	1.16	12.2	..	4.7	30
Lebanon	-31.1	11.5	-17.4	4.5	12.88	16.3	11.8	26.7	..
Morocco	17.1	2.6	-2.7	0.48	..	17.3	..	14.4	35
Syrian	16.3	6.1	-0.4	1.6	..	12.9	17.3	23.8	..
Turkmenistan	18.6	-3.9	..	..	-0.02	14.3	..	..	..
LIC									
Albania	-14.4	0.4	-10.4	2.0	8.38	14.8	..	20.4	..
Azerbaijan	12	-7.4	-4.7	..	..	11.0	18.0	3.5	31
Bangladesh	13.4	4.9	..	..	..	4.5	..	..	..
Benin	4	4.5	..	..	..	10.5	..	..	..
Burkina Faso	8.5	3.8	1.2	..	..	15.0	..	30.8	..
Cameroon	19	0.4	-2	2.2	0.22	10.6	10.4	28.2	39
Chad	-1.4	2.1	-4.9	5.2	..	9.4	..	14.9	..
Comoros	-3.7	0.1	..	..	..	15.2	..	..	..
Djibouti	-10.5	-2.1	..	..	..	37.2		..	..
Egypt	13.4	4.5	-1.4	-0.9	2.31	10.5	..	35.8	40
Gambia	4.9	3.3	-0.8	..	..	14.0	..	6.4	..
Guinea	14.2	4	-3.2	3.6	-0.31	9.3	10.9	14.2	..
Guinea-	1.2	1.2	..	..	..	8.4	..	..	..
Kyrgyz	4.8	-3.4	-6.1	3.5	2.97	20.0	..	13.5	30
Maldives	25.2	7.7	-9.6	5.3	..	30.3	..	43.0	..
Mali	7.7	3.2	..	..	..	12.0	..	..	..
Mozambique	-6.6	5.6	..	..	..	10.5	..		35
Niger	2.7	1.9	..	..	2.78	14.6	..	..	..
Oman	28.2	6.2	-7.3	4.6	4.93	33.4	8.1	73.6	21
Pakistan	12.1	4	-7	2.0	..	12.6	..	25.0	..
Senegal	10.1	3.3	..	..	..	12.7	..	..	35
Sierra Leone	1.8	-4.1	-4.7	3.7	..	10.6	8.9	3.9	..
Suriname	21.3	3.1	..	..	..	33.0	..	..	..
Tajikistan	15.1	1.6	-2.5	2.3	1.42	10.3	..	3.3	..
Togo	7.3	1.7	..	..	7.04	13.0	..	..	..
Uganda	3.8	6.9	..	..	5.91	9.6	..	..	30
Yemen	7.2	3.1	-7	1.1	..	18.4	..	51.2	

Source: WDI, World Bank, 2002

Many IDB member countries experienced large fiscal imbalances throughout the 1990s. Fiscal imbalance is defined as the inability of the governments to raise sufficient funds to meet their obligations. For the majority of IDB member countries, overall fiscal policy was expansionary in the 1990s due to, among other things, high social spending. Consequently, the public sector in the majority of the IDB member countries registered fiscal deficits ranging between an annual average of 0.4 per cent and 17.4 per cent of GDP. Specifically, more than half of the IDB member countries exhibited, on average, an annual fiscal deficit exceeding 3 percent of GDP during the same period. Owing to unproductive public spending, these persistent fiscal deficits tended to crowd out private investment by reducing the stock of credit available to the private sector in many IDB member countries. The calculated cross correlation coefficient between the fiscal balance and the gross domestic saving (0.64), may suggest that improvement in the fiscal balance is likely to be associated with a corresponding boost in savings, mainly as a result of an increase in public saving. Accordingly, the useful observation that deserves to be made is that prudent fiscal policy can be seen a prerequisite for promoting public savings in the IDB member countries.

The fiscal conditions in many member countries seem to suggest that there is a scope for better fiscal management to achieve macroeconomic stability and enhance domestic resource mobilization. Yet, the main challenge for member countries is to find innovative ways to boost both private and public savings to be able to sustain a level of domestic investment compatible with the required poverty-reducing growth. Additional resources from the proceeds generated by good privatization programs can also contribute to alleviating fiscal constraints in many IDB member countries.

3.2.3 Privatization as a source of additional resources

Privatization has become a truly global phenomenon, whereas a number of active programs for transferring state assets to the private sector are under way in many countries. Despite the prospects for fiscal consolidation and higher public savings, through a further reduction in the size of the state sector, only few IDB member countries have so far made significant strides in their privatization programs. More than 90 percent of the cumulative proceeds from privatization during the whole decade accrued to these member countries (Table 3.3). The structural reforms currently under implementation in these countries were directed towards reducing the size of the government sector, with a progressive shift towards privatization of government enterprises, and enhancing the role of the private sector in production activities. For exemple, The sale of 30 percent stake in Societe Marocaine des Industries du Raffinage (SAMIR) in Morocco to the Swedish investor contributed to the increase in privatization revenues (see Box 3.2). Equally, the permission for foreigners, for the first time, to purchase stakes of more than 50 percent in public enterprises also contributed to the success of privatization in Egypt. Although privatization can be an important source of financial resources for development, IDB member countries have to strike a balance between generating revenues through privatization, and the issue of allowing important sectors of the economy to be owned totally by foreign

companies. Meanwhile, in Sub-Saharan Africa, $299 million of the sum of $623 million in privatization were raised through sales to foreign investors (ECA, undated).

Box 3.2: A Privatization Success Story: Morocco's Telecommunications Sector

Morocco's privatization began in late 1989, when the Parliament adopted a privatization law. The programme presented an initial list of 112 public enterprises that were to be privatized by 1995.

Guaranteeing the transparency and accountability of the privatization programme has been a major goal. Towards this end, operating responsibilities have been separated, and careful attention has been paid to oversight. An inter-ministerial Transfer Commission, appointed by the King, advises the ministry on privatization strategies for different enterprises and on the selection of bidders for open tenders and private placements. An independent Valuation Authority reviews the valuation of enterprises and sets minimum prices. Although the process has not been perfect, there is a general consensus among local and foreign investors that it has been conducted openly and professionally.

The privatization of telecommunications has been hailed as a success story for its exemplary openness and transparency. The government began to liberalize the sector in 1999 by awarding a mobile telecommunication licence through international tender-challenging the monopoly of the state-owned Maroc Telecom. The winner, Medi Telecom, paid US$1.1 billion, one of the highest prices ever paid for a mobile license relative to population size. This transaction was followed by the sale of 35% of Maroc Telecom for US$2.1 billion in December 2000.

Getting privatization "right" put Morocco on the radar screen of foreign investors and enabled it to reap big rewards. In what ways did Morocco get it right? By establishing a credible regulatory framework, ensuring transparency in the tendering process, and making the terms of the license attractive.

The new license has already led to lower prices and better services. It also promises higher revenues for the government and new job opportunities. The US$1.1 billion license fee boosted financial revenues by 13% in 1999-and according to Wellenius and Rossotto (1999), total fiscal benefits (including future taxes and research and development) could be much larger, between US$2 billion andUS$3.5 billion by 2008 in present value terms. Medi Telecom expects to employ around 3,000 people, and its operations may generate additional 20,000 jobs.

Source: ECA, 2002.

In previous decades, the public sector emerged as the main engine for growth in the economy. For instance, in the early 1990s, public sector investment in the IDB member countries from the Arab region amounted to about half of total investment, compared to 38 percent in developing countries and 17 percent in OECD countries (World Bank, 2001). During the second half of the 1980s, public enterprises accounted for almost 40 percent of economic activity in Egypt, 35 percent in Tunisia, and 20 percent in Morocco compared to an average of 10 percent for middle income developing countries.

Table 3.3 Privatization Proceeds and Saving (1990-1999 Averages)

Country	Gross Domestic Saving Ratio	Gross National Saving Ratio	GDP Growth Rates	Privatization (US$ Million)
Algeria	30.2	28.4	1.3	18.4
Bahrain	37.2	16.8	3.9	150.6
Gabon	41.7	26.8	2.8	..
Iran	26.7	27.6	4.8	..
Kuwait	10.8	5.5	10	..
Malaysia	40.6	34.7	7.2	1128.8
Saudi Arabia	29.8	20.1	2.8	0
Tunisia	23.9	24.0	5.1	65.4
Turkey	20.4	24.3	3.8	465.4
UAE	36.2	..	3.8	..
MIC				
Indonesia	32.3	28.8	4.8	613.5
Jordan	4.6	23.9	4.9	12.8
Kazakhstan	18.2	16.0	-5.3	1062.7
Lebanon	-31.1	2.7	11.5	..
Morocco	17.1	21.0	2.6	387.8
Syrian	16.3	11.9	6.1	..
Turkmenistan	18.6	13.0	-3.9	..
LIC				
Albania	-14.4	8.8	0.4	9.5
Azerbaijan	12	11.0	-7.4	7.9
Bangladesh	13.4	20.6	4.9	8.5
Benin	4	7.7	4.5	7.8
Burkina Faso	8.5	17.8	3.8	1.9
Cameroon	19	13.6	0.4	33.3
Chad	-1.4	6.2	2.1	..
Comoros	-3.7	11.1	0.1	..
Djibouti	-10.5	..	-2.1	..
Egypt	13.4	22.2	4.5	484.2
Gambia	4.9	14.4	3.3	..
Guinea	14.2	14.6	4	45
Guinea-Bissau	1.2	8.7	1.2	0.1
Kyrgyz	4.8	4.2	-3.4	69.8
Maldives	25.2	13.2	7.7	..
Mali	7.7	15.3	3.2	11
Mozambique	-6.6	2.0	5.6	15.4
Niger	2.7	2.1	1.9	..
Oman	28.2	4.8	6.2	10
Pakistan	12.1	20.2	4	221.4
Senegal	10.1	..	3.3	136.9
Sierra Leone	1.8	..	-4.1	1.6
Suriname	21.3	38.1	3.1	..
Tajikistan	15.1	15.1	1.6	..
Togo	7.3	12.1	1.7	6.4
Uganda	3.8	8.0	6.9	19.4
Yemen	7.2	10.8	3.1	..

Source: WDI, World Bank, 2002

The public sector continues to dominate economic activity in many IDB member countries as reflected in the much slower rate for privatization. This slow take-off of private activity could largely be explained by political influence, bureaucratic resistance, and the vested interest in the public sector and state-owned enterprises as major sources of secured employment.

This limited role of the private sector in economic activity is also reflected in the data presented by the World Bank Private Participation in Infrastructure database (World Bank, 2000). The database tracked 1700 private, newly-owned or managed projects that reached financial closure between 1990-98 in various sectors such electric power, telecommunications, and the transportation sectors. Among these projects, the value of projects in member countries from the Arab region was a small fraction of $500 billion, or approximately 2.6 percent. Most of those projects were 'green field' projects or operations and management contracts with major capital expenditures.

Divestitures were also minimal during that period reflecting, again, the continued dominance of the public sector in the region. Proceeds from privatization for the IDB member countries as a group ranged between about US$ 1 billion in 1991 and nearly US$9 billion in 1997. Table 3.3 shows that on average, privatization proceeds accruing to individual member countries ranged between less than $US 1.00 million (Guinea-Bissau) and $US 1.13 billion (Malaysia).

To sum up, one can say that the overall privatization picture is not uniform across IDB member countries. In some member countries, the pace is picking up while in others privatization programs are just beginning or have slowed. For instance, as of 1999, cumulative privatization proceeds per capita were US$0.5 million in Bangladesh, US$0.7 million in Burkina Faso, US$0.3 million in Sierra Leone, US$452 million in Bahrain, US$447 million in Malaysia, and US$427 million in Kazakhastan. As a share of GDP, cumulative proceeds ranged between 40 per cent (Kazakhastan) and 0.11 per cent (Mauritania).

3.3 Financial Sector Development and Resource Mobilization in IDB Member Countries

3.3.1 The importance of financial sector development for resource mobilization

The importance of the financial sector in promoting economic growth was recognized as early as Schumpeter (1912). Since then, there has developed a large and growing body of literature that examines the relationship between financial market development and various economic outcomes. So far, the empirical evidence suggests a positive first-order relationship between financial development and economic growth. The level of financial development is perceived to be a good predictor of future rates of economic growth, capital accumulation, and technological change (King and Levine, 1993). Rajan and Zingales (1998) claim that financial development affects growth by reducing the differential cost of external finance. Nonetheless, the role of the financial system is essentially

mobilizing financial savings and channels them to the most effective potential users.

Financial development can help strengthen bank intermediation and diversify the range of financial instruments available to savers and investors. Countries that have more developed stock markets and/or deeper banking systems are more likely to grow fast. Equally, well-established capital markets with suitable regulatory and monitoring capacity are crucial for overall resource generation. It is only the efficiency of the financial system which determines whether the full potential of resources has been mobilized at any particular stage of development.

A joint initiative undertaken by the World Bank, the IMF and other national development agencies known as Financial Sector Reform and Strengthening Initiative (FIRST) is a significant new multi-donor programme, supporting capacity building and policy development projects in the financial sectors in developing countries. The World Bank and the IMF will play a key role in identifying and introducing projects for FIRST and providing expert advice in policy-related areas (see Box 3.3).

Box 3.3: Financial Sector Reform and Strengthening (FIRST) Initiative

FIRST provides technical assistance grants to low and middle-income countries for short and medium-term capacity building and policy development. By strengthening national financial sectors, FIRST will support economic growth and, in turn, poverty reduction. This will also contribute to crisis prevention and the establishment of a more stable international financial system. As an example, countries that wish to improve financial supervision or accounting standards would be able to seek FIRST funding to achieve these reforms.

Project results in one country under the FIRST initiative will be used or adapted in others, saving money and providing developing countries with a much more coordinated approach to financial sector assistance.

The World Bank and the IMF have undertaken assessments of over 60 developing countries through the Financial Sector Assessment Program (FSAP) or the program of Reports on the Observance of Standards and Codes (ROSC). Many developing countries, however, do not have the resources or expertise to follow up on the findings of these programs. FIRST offers such countries the assistance they need.

FIRST will allow the international community to help countries set priorities, mobilize expertise and financial resources, and provide effective technical assistance in a cost efficient way.

In addition, FIRST will play a key role in the co-ordination of donor activity in the financial sectors of developing countries by establishing an information exchange on the delivery of financial sector technical assistance in developing countries. Participants in FIRST are:

The UK Department for International Department (DFID) (up to US$29,000,000), the International Development Agency of Canada (CIDA) (up to US$7,500,000), and the State Secretariat for Economic Affairs of Switzerland (SECO) (up to US$8,000,000). In addition to its staff, the World Bank has agreed to contribute up to US$500,000 to the initiative. The International Monetary Fund will provide in-kind assistance. Discussions are in progress with other bilateral donors and international financial institutions with the aim of expanding the scope of FIRST.

Source: IMF, 1999

Similarly, IFC's experience with financial capacity building projects and the lessons learned are also worth-noting. Table A3.1 in the Annex shows the impact of some of IFC projects on mobilizing and allocating savings and the lessons learned. IFC, as an affiliate of the World Bank, has focused on supporting the growth of domestic private investment, through the direct support of local entrepreneurs and through development of domestic capital markets.

3.3.2 Financial markets

The institutional frameworks for the mobilization of financial resources in many IDB member countries are not sufficiently well developed to achieve the full potential of savings, promote investment and thus generate high economic growth. Table 3.4 shows different measures of financial development in IDB member countries. When the ratio of M2 to GDP is used to gauge the level of financial development in IDB member countries, financial development in these countries averaged less than 50 percent over the last decade. This is a clear evidence of the lack of depth of the financial sector in many IDB member countries. Meanwhile, the limited range of financial institutions, the low density of geographical expansion, and the quality of regulation and supervision reflect this lack of depth. Additionally, more than half of these countries do not have an official stock market. Consequently, consistent financial liberalization and reforms in many of the IDB member countries, remain a critical policy challenge, particularly in the context of growing financial innovation and globalization.

The data in the table also shows low or missing market capitalization for many IDB member countries, relatively low liquidity rates, and very low rates of credit to the private sectors. These figures confirm the lack of financial development in the IDB member countries. Meanwhile, the ability of a country to mobilize domestic savings to finance investment activities depends in part on its level of financial development: the lower the level of a country's development, the fewer domestic resources it mobilizes to finance private investment activities.

Only few IDB member countries have a well-established capital market that has grown in scope and content over the past several years. In recent years a number of IDB member countries have started organizing their own capital markets. However, these capital markets still lack the proper depth and breadth needed to enhance the efficiency of their operations and the information flows required to bring discipline and orderliness. Additionally, a number of over-the-counter exchange facilities (OTCs) have been established, and both primary and secondary markets trading have been growing in these capital market over the past few years (see Table A3.2 in annex). Yet, there is much more that needs to be done to regulate and discipline member countries' stock market operations. The inadequate information systems and the delays in settling transactions continue to impede the operational efficiency of these new stock markets.

Table 3.4 Saving and Financial Sector Development (1990-1999 Averages)

Country	Gross Dom. Saving Ratio	GDP Growth Rates	Credit to Private Sector	Liquid Liabilities	Real Interest Rate	Market Capitalization % GDP	Traded Stocks %GDP
HIC							
Algeria	30.2	1.3	12.8	48.5	1.8	..	..
Bahrain	37.2	3.9	85.5	71.3	..	126.5	..
Gabon	41.7	2.8	10	16.1	15.5	..	..
Iran	26.7	4.8	28.5	47.3	..	10.9	1.3
Kuwait	10.8	10	47.3	101.6	5.6	61.7	..
Malaysia	40.6	7.2	117.5	106.1	4.7	195.4	..
Saudi Arabia	29.8	2.8	61.6	51.3	..	38.2	6.3
Tunisia	23.9	5.1	63.7	50.3	..	11.8	1.2
Turkey	20.4	3.8	19.9	32.8	..	20.5	..
UAE	36.2	3.8	45.2	51.8	..	70.5	..
MIC						..	
Indonesia	32.3	4.8	48.1	48.2	7.7	22.2	..
Jordan	4.6	4.9	70.9	110	5.7	68.5	11.3
Kazakhstan	18.2	-5.3	15.8	13.7	..	9.4	..
Lebanon	-31.1	11.5	60.1	141.2	3.6	12.3	..
Morocco	17.1	2.6	44.8	70.7	7.8	20.2	..
Syrian	16.3	6.1	9.5	55.2	..	..	..
Turkmenistan	18.6	-3.9	3.2	16.3	..	..	..
LIC						..	
Albania	-14.4	0.4	3.7	51.4	-12.9	..	..
Azerbaijan	12	-7.4	4.2	25.5	-71.9	0.1	..
Bangladesh	13.4	4.9	19.1	27.7	10.0	3.0	..
Benin	4	4.5	11	26.4	14.1	..	..
Burkina Faso	8.5	3.8	11.3	22.9	18.5	..	..
Cameroon	19	0.4	13	17.4	14.9	..	..
Chad	-1.4	2.1	4.6	12.5	13.9	..	..
Comoros	3.7	0.1	14.6	22.1	..	..	..
Djibouti	-10.5	-2.1	46.6	69.6	..	..	..
Egypt	13.4	4.5	38.2	85.4	6.4	16.4	..
Gambia	4.9	3.3	10.8	25.7	20.6	..	..
Guinea	14.2	4	4.2	7.8	10.1	..	..
Guinea-Bissau	1.2	1.2	11.2	24.4	0.7	..	..
Kyrgyz	4.8	-3.4	7	14.5	30.8	0.2	0.0
Maldives	25.2	7.7	19.4	47.4	..	..	..
Mali	7.7	3.2	13.2	22.5	12.9	..	..
Mozambique	-6.6	5.6	14.2	25.9	19.4	..	..
Niger	2.7	1.9	7.4	14.1	18.5	..	..
Oman	28.2	6.2	28.9	31.5	9.5	20.4	..
Pakistan	12.1	4	27.1	44.8	..	15.6	9.8
Senegal	10.1	3.3	20.6	23.2	15.4	..	..
Sierra Leone	1.8	-4.1	2.8	12.5	-0.2	..	..
Suriname	21.3	3.1	29.2	76.3	-29.4	..	..
Tajikistan	15.1	1.6	..	..	..	..	..
Togo	7.3	1.7	21.4	29.1	13.1	..	..
Uganda	3.8	6.9	4.9	11.7	10.0	..	..
Yemen	7.2	3.1	5.2	46.8	6.4	..	..

Source: WDI, World Bank, 2002

3.3.3 The banking sector

The banking sector continues to dominate as the major savings/investment conduit in all financial markets in the IDB region. Equity markets and bond markets in the IDB member countries are small compared to the size of the banking sector. Therefore, the health of the banking sector is central to the ability of countries to mobilize their domestic resources for development. Meanwhile, there are many factors impeding the efficiency of the banking sector in the IDB member countries. First, state-owned and often insolvent banks are still quite dominant in the many IDB member countries. In order for these banks to play a much more important role, both their financial infrastructure and their assets structure should be improved to make them attractive for potential buyers. Second, the development of a broader financial market has been proceeding at a very slow pace. Fragmented markets characterize many countries where the informal financial markets play a very dominant role. Third, banking services are concentrated in urban areas without providing access to rural areas. Other major problems include the lack of a competitive environment and the excessive lending risk.

The banking sector in the region has undergone considerable restructuring over the last two decades. In some member countries, the banking services have been modernized and information technology is widely used. As a result of the deliberate efforts to liberalize the banking sector, a significant shift in the ownership pattern occurred. There have also been regulatory and supervisory reforms to solve the non-performing loans (NPLs) problems. Although, there has been considerable progress region-wide, there are still a number of outstanding issues to be tackled.

The structure of the banking sector varies considerably across countries. While some countries (e.g., Malaysia), have a relatively small number of major banks, mainly privately-owned, other countries (e.g., Pakistan), are characterized with a relatively small number of banks, with the major ones are publicly-owned. In Indonesia on the other hand there is a larger number of relatively small banks, usually private ones. The reasons for these varying structures are often historical and are directly influenced by the bank licensing policies of the government.

The financial sector in most member countries are considerably underdeveloped and weak. For instance, African member countries are, in general, less financially developed in terms of selected quantitative indicators in comparison to world norms. Financial weaknesses in these countries are due, in part, to distortions arising from the need to finance large government budget deficits or to direct lending to state-owned enterprises. State banks in these countries are usually afforded preferential treatment, often in terms of tax concessions and access to public-sector deposits. This can thwart competition and reduce efficient bank intermediation. The poor quality of bank supervision has also led to NPLs being understated and banks being insufficiently capitalized. Reform and liberalization of the financial systems of some of these countries is under way, but enforcement of key legislation remains weak in many of them.

The ownership structure of banks in some of the member countries has changed in the last few years due to financial liberalization. Allowing foreigners to own equity stakes in banks, finance and security firms has generated significant inflow of FDI to these countries. There has been a similar but slower liberalization of ownership of banks in the other economies of the region. Yet, there are arguments for and against an increased foreign ownership of the banking sector. While foreign competition can increase pressure for consolidation and modernization and for the introduction of new products and services, there can also be a flight to quality as domestic clients might prefer to deal with banks having foreign participation, leaving domestically owned banks to service less attractive and more risky segments of the market. This could negatively influence the financial viability of the latter institutions.

The importance of banks in providing commercial lending in some member countries is slowly declining, while the role of capital (stock and bond) markets is increasing in importance as a modality for mobilizing domestic funds. This is partly the result of a deliberate government policy to increase the stability of the economy through the diversification of modalities to finance investment. In the long run, banks should assume a less dominant role in the financial structure and learn how to cope with competition from a more diversified set of institutions.

In most member countries, irrespective of their levels of development, there are publicly owned specialized banks with a distinct focus on a specific sector, such as agriculture or housing. These banks often have an important role to play in mobilizing savings (and intermediating these into investment) in sectors which are of little or no interest to commercial banks. The promotion of these specialized banks needs to be undertaken with care so that they operate as closely as possible on commercial terms while servicing their particular clients. In most cases,, these specialized banks play an important anti-cyclical role in the economy, encouraging savings and making loans when other banks are reluctant to do so.

In many countries both public and private banks have extended their geographic coverage within national borders over the past decade, thus providing savings opportunities to a wider proportion of the population. The increased use of information technology in the banking sector, particularly the use of ATMs (automatic teller machines), has accelerated this development. However, there is a genuine need in several member countries for expanding the banking networks, including electronic banking, where such services are mainly urban-based. Banks have not catered well to the needs of the poor, the remote, the landless, the asset-less, or the dispersed population, nor of SMEs and the informal sector.

3.3.4 Rural finance and resource constraints

Some 75 per cent of the world's poor currently live in rural areas, and rural poverty is likely to predominate for decades to come (IFAD, 2001). Notwithstanding the growing urban population, the proportion of the rural population still remains dominant in both low and middle income member countries (Table 3.1). In other

words, most of the poor are to be found mainly in rural areas, particularly for the LDMCs. For example, 88 per cent of the population in Uganda is rural.

In this context, more attention is to be directed towards the rural areas with a view to finding effective ways to promote rural savings, perhaps through a system of financial intermediaries at the grass roots. The rural financial systems have to be developed if the rural population is to be provided with cost-effective and higher quality facilities for savings deposits and credit (see Box 3.4). The informal financial sector performs a noteworthy role in these areas and should, therefore, be encouraged, diversified and integrated into the formal financial sector institutions. Both sectors should expand and develop hand in keeping with the common objective of maximizing the mobilization of domestic savings, thus reducing the reliance on external sources. This would mean adopting a savings/deposits-led approach as opposed to the supply-led strategy of the past.

One feature of the banking system that deserves special attention in some IDB member countries is rural finance. Conscious efforts are being made in some LDMCs to spread banking facilities to the rural sector in order to facilitate development and diversification of the activities in the rural economy (for further details see chapter IV, Section 4.2).

Recently, a number of mechanisms for concessional resource transfers to developing countries have been explored with a view to providing financing to the rural sector. One good example is the Italian Debt Swap initiative, under which Italy has cancelled official debts in countries like Egypt, where the resources released are to be used for poverty eradication

The overriding policy goal of governments in the IDB member countries is to expand rural incomes and reduce poverty in rural areas through a favorable policy environment and more agricultural credit. The declining trends in investment in the rural sector must be reversed if the Millennium poverty goal is to be achieved. In addition to mobilizing domestic savings, external resources originating from FDI, trade exchanges and development assistance can play a significant part in launching and sustaining this development process in many member countries.

Generally a larger share of rural credit comes from private sources. Moreover, even as the international focus on poverty has strengthened over the last decade, the share of ODA going to agriculture and the rural sector, where most of the poor live, has decreased. The volume of ODA for agriculture in developing countries has fallen by nearly 50%, from $US4.9 billion in 1988 to $US 2.5 billion in 1999 (IMF, 2000). Almost all multilateral financial institutions have reduced lending to agriculture. For example, the World Bank lending to agriculture went down from 25 per cent of its total lending two decades ago to about 7 pre cent or $US 1.1 billion in 2000 (IFAD, 2002).

Box 3.4: The FAO and Rural Finance

Safeguarding Savings Deposits

The FAO has initiated a programme called 'Safeguarding Savings Deposits' which is designed to address the issue in the light of an analysis of recent experience both in developed and developing countries. Its objective is to draw on the findings to develop guidelines and training materials, primarily for grassroots level rural financial intermediaries in developing countries.

Reform of Agricultural Development Banks

FAO, together with other development agencies such as IFAD, is developing a methodology for the reform of agricultural development banks.

Role and Importance of Collateral in Rural Lending

Lack of acceptable collateral is often quoted as one of the main reasons for not granting loans to certain categories of potential borrowers which traditionally include small scale farmers and other rural entrepreneurs, and more recently private traders who are increasingly assuming a major responsibility for marketing of agricultural produce. Another problem faced in many countries is the fact that only a very low percentage of the actual value of the pledged property is accepted as collateral.

Reasons for the latter situation can be the uncertainties of the valuation of the property, as well as the difficulties in seizing and liquidating the collateral, either due to an inadequate legal framework or a specific social environment. On the other hand, limited lending in rural areas particularly to small enterprises and small scale farmers might be due to the general mistrust and assumed high risk commonly connected with this category of borrower, as well as higher than normal transaction costs caused by a large number of very small transactions.

FAO has initiated a programme for designing methods for removing some of the main collateral constraints, and/or for permitting existing collateral to be used more effectively. This programme will also look into alternative ways for securing loans, particularly in the case of less affluent customers. The work is being carried out in close collaboration with the Regional Agricultural Credit Associations and ALIDE.

Automation of Rural Finance Operations

FAO has developed a low-cost software system, called the FAO Micro Banking System, designed to run on basic PC equipment. It is flexible in that it can cater for a single teller, with stand-alone installation, as well as for a multi-teller installation of up to ten windows. It is a front-office system, which means that data are entered at the time of the transaction. The software caters for various internal checks and a series of management reports. As of August 1999, the FAO Micro Banking System was running in over 1100 sites in Asia, Africa, Central and Latin America, Russia and Central and Eastern Europe.

Training in Rural Finance

The need for new paradigms in rural finance has emerged from several developments:

1. The globalization of world economy and the economic integration that is taking place is creating a new operational environment for production, distribution, trade and commerce.
2. The Basle Committee norms on prudential norms such as capital adequacy, income recognition, provisioning, asset valuation, which have been by and large adopted by mainstream commercial banks and financial institutions, and which over a period will have impact on the functioning of the rural financial institutions as well.
3. The growing fiscal constraints in many countries is leading to sizeable cuts in the budgetary allocations of the rural financial institutions, thereby leading them to interact to a greater extent with market related institutional structures in respect of resource mobilization etc.,
4. Developments in technology and communications are bringing out rapid changes in the perceptions of the people on important aspects of rights, responsibilities and obligations. These developments are also facilitating faster network among people, products and the institutions.

The new paradigms on rural finance training thus calls for adequate focus on (a) networking (b) building relationships (c) promoting of a greater degree of interaction and (d) effective communication.

FAO currently revises its Rural Finance Training in order to address all major actors in rural finance, particularly: A) Policy Makers/Central Banks/Representatives of People/Opinion Makers; B) Financial Institutions; C) Clients/Customers/Rural Households/Firms/Farms/Businesses

Source: FAO, 2000

3.3.5 Islamic finance and resource mobilization

Since Islamic finance has become a reality in many IDB member countries, its role in mobilizing resources warrants investigation[2]. Islamic banking industry has grown significantly over the past 20 years, both in the amount of funds mobilized and the number of institutions that span more than 40 countries worldwide (see, Dhumale and Sapcanin, 2001). Being one of the fastest growing industries, Islamic finance has an important role to play in resource mobilization. In particular, Islamic banks can appeal to the majority of depositors and small savers in IDB member countries who shun away from interest-based conventional banks. As often said by Islamic economists, the "goal of mobilization of savings is essential because Islam condemns the hoarding of savings and urges for their productive use for the realization of the socio-economic goals of Islam" (Chapra, 1985).

Since the majority of poor people in IDB member countries live in the rural areas, Islamic banking can play a major role in financing the poor and greatly affecting their lives through the development of microfinance programs. The potential of small-scale enterprises as engines for growth and poverty reduction is receiving increasing attention. Meanwhile, the formal financial sector has played a minimum role in financing SMEs in the IDB member countries. According to a recent World Bank's survey, only one commercial bank-Egypt's National Bank for Development- is active in microfinance industry. It is well documented that there has been a sectoral and geographical contraction of the outreach of the banking services in the IDB member countries, particularly in rural areas. By creating cooperative units or expanding their branches in the rural areas, Islamic banks can be instrumental in rural development. The development of rural Islamic banking facilities can alleviate shortage of credit in the rural sector, where the majority of the populations live.

As a development institution, the IDB can play a crucial role in the development of Islamic banks in rural areas. For instance, through its various schemes (Islamic Banks Portfolio for Investment and Development (IBP), IDB Unit Investment Fund, etc.) the IDB can raise additional resources with a view to strengthening its operations in the member countries. Likewise, the Islamic Corporation for the Development of Private Sector (ICD) intends to play an active role in providing additional resources for private investors in member countries.

The number of Islamic banks and financial institutions have increased to more than 180 by the end of 1996. Over the period of 1985-1995, the number of Islamic banks and financial institutions has increased more than sixfolds. 47 Islamic banks and financial institutions are established in South Asia, 30 in Africa, 24 in South East Asia, 22 in the Middle East, 17 in the GCC Countries and at least 4 in Europe and America. If Islamic funds managed by conventional banks are accounted for, Europe and America's share of Islamic financing would be higher (Kahf, 1999).

As table 3.5 shows, in 1995, the total capital of the 144 banks was slightly above US$6 billion, while their total assets reached US$166 billion. The total deposits of these banks surpassed the amount of US$77 billion, their reserves were around US$3 billion and the net profits reached nearly US$1.25 billion.

In terms of modes of financing and according to the 1995 figures of the International Association of Islamic Banks, the murabaha mode (sale-based) accounts for 45% of the total value of operations, while musharaka accounts for 15% and mudharaba 9% and 10% for Ijara (leasing) (Kahf, 1999).

It is also believed that there is a great deal of unused financial potential in rural areas. Even the poorer members of the population may have some savings either in the form of real assets or monetary savings. But because of the lack of a reliable financial infrastructure, these savings are not channeled into productive use. Islamic banks can have an important role to play in mobilizing rural savings (Box. 3.5).

The development of such instruments can foster the development of money markets and deepen them. However, institutional arrangements for interbank and secondary markets need to be supported by efficient payments and settlement systems and well designed bank credit facilities. In the area of financial innovation and emergence of new financing instruments, the Islamic Development Bank (IDB) pioneered the securitization development with its Unit Investment Fund (UIF), which was launched in 1990. The UIF is an open-ended fund consisting of Ijara, installment sale, and Murabaha contracts that are contracted by the Bank.

Several countries have developed project-specific funding instruments by applying the principles of Mudharaba or Ijara[3]. At present, general purpose government funding papers are issued only in Malaysia under the Government Investment Issues (GII) scheme. The purchase of GII by investors is considered benevolent (Qard Hassan) made by the public to the government. The providers of funds do not expect any return, but do expect the principal amount to be paid back at maturity. The GII instrument was primarily used to comply with the liquidity requirement of the Central Bank of Malaysia. Other monetary instruments have also been suggested (Haque and Mirakhor, 1997) to finance government operations, in particular infrastructure projects (Box 3.6).

Table 3.5: Islamic Banking and Financial Institutions: Summary of Financial Highlights, 1995 (US$ '000' S)

REGION	No. of Banks*	%	CAPITAL		TOTAL ASSETS		DEPOSITS		RESERVES		NET PROFIT	
			Amount	%	Amount	%	Amount	%	Amount	%	Amount	%
South Asia	47	32	951,194	15	45,269,061	27	26,413,855	34	1, 012,689	34	365,301	29
Africa	30	21	257,476	4	3,794,394	2	2,112,960	3	112,149	4	32,517	3
South East Asia	24	17	121,919	2	1,736,361	1	1,342,604	2	101,957	4	20,570	1
Middle East	22	15	3,310,506	53	97,209,926	59	29,693,917	38	596,476	20	149,798	12
G.C.C.	17	12	1,464,846	23	17,648,197	11	16,571,459	21	1,050,278	36	655,367	53
Europe & America	4	3	201,875	3	395,219	0	1,381,037	2	65,446	2	21,940	2
TOTAL	*144*	*100*	*6,307,816*	*100*	*166,053,158*	*100*	*77,515,832*	*100*	*2,938,995*	*100*	*1,245,493*	*100*

Source : International Association of Islamic Banks;* IDB is not included.

Box 3.5: The Role of Islamic Banks in Rural Development

Mobilization of Rural Savings

Before Islamic banks enter the field for collecting savings from rural households, they would need legal and administrative support from their governments. A suitable legal framework would be necessary for:

- Creating and regulating saving societies at village level. In some countries, cooperative societies already exist, but they are either dormant or are not properly regulated. Therefore, they do not enjoy the confidence of the people. This confidence would have to be ensured before any meaningful campaign was launched to collect rural savings.
- Organizing the work of cooperative or saving societies on a profit-loss-sharing basis. In all probability, the savings would be mobilized on two accounts: current account, which does not earn any return: and investment account, which participates in the profit or loss of the society.

It would not be possible, of course, for Islamic banks to open branches in every village. But they should be able to establish links with village cooperative societies, or saving societies. The banks could encourage these societies to place their funds with them on a profit-loss-sharing (PLS) basis. This would also bring some return to the savers.

Setting Up Rural Investment Trusts

Islamic banks could take the initiative in setting up Rural Investment Trusts. These trusts would hold funds on behalf of the rural population and issue Investment Trust Certificates. These certificates would be readily cashable at the banks, branches. The banks would invest these funds in agro-businesses and rural industries. Investment Trusts are not new. They are already in vogue in many countries. The only innovation is that Islamic banks should move into the rural sector and persuade people to deposit their funds with them for investment purposes. The Investment Trusts would provide the hitherto untapped financial resources for investment in rural areas.

Managing Remittances from Abroad

A number of countries receive regular remittances from their citizens employed abroad. These remittances remain deployed in urban areas although most of the people who send these funds belong to rural areas. Islamic banks could offer to provide quick remittances to workers' families locally. Of course, Islamic banks would also have to establish contacts with the remitting banks abroad. Islamic banks could further persuade workers to remit money through them by announcing that these funds would be used for uplift of the very areas to which these workers belong. For their part, Islamic banks could set up Remittance Funds to finance and refinance, on a PLS basis, commercial and industrial projects in rural areas. The remittances would, thus, also earn a return from these investments.

Managing Small Industries Fund for Rural Areas

There is a great need to promote small-scale industries in rural areas. These areas produce most of the raw materials for industries but processing of the raw materials is done in urban centers. To encourage location of industries in rural areas, financial support, and the wherewithal, is necessary. Islamic banks could establish Rural Industries Funds where rural people could deposit their savings for investment in rural industries on the basis of PLS. The savers would be able to earn a return on their deposits and have the satisfaction of knowing that their funds will be invested in their own areas. It would have the effect of generating employment opportunities in rural areas. The initiative to pool rural savings for investment in rural areas would also overcome a historical injustice as regards the rural population. It has been estimated that approximately 25% of the rural population's savings remain in rural areas. The remaining flows to national and international commercial banks.1 However, the banks do not provide credit 10 rural people easily as, according to them, 'they do not have good projects or adequate collateral'. Thus rural savings are at present a mechanism to further benefit the urban rich.

Managing Zakah and Ushr Funds

Islamic banks could also offer to manage Zakah and Ushr funds on behalf of the local community and government. They could collect, disburse, invest, and control Zakah funds. This would reduce the cost of managing these funds for the local community. Although the banks could charge for their services, where possible they could provide these services free.

Source: Adapted from Muhamad Akram Khan, Rural development Through Islamic Banks, the Islamic Foundation, 1994

Box 3.6 Participation Papers in Iran (Restricted Mudharaba) Issued Since 1993

In the restricted Mudharaba framework, commercial banks act as agents to raise funds to finance a specific investment project. The borrower provides market and financial analyses of the project, which include an expected return that it is prepared to share with lenders[4]. The commercial bank undertakes an initial economic review of the proposal and its terms to determine its accuracy and reasonableness. If approved, the credit committee also sets a guaranteed minimum return that will be paid to investors. It is expected that the actual rate will be higher than the minimum. In addition, the principal is also guaranteed by the commercial bank. To ensure payment of the guarantees, the following steps are taken:

- The proceeds of the Participation Papers (PPs) are placed with the agent-bank
- Additional collateral is obtained in addition to cash deposits.
- The central bank appoints an auditor and trustee to protect the interests of the investors.

PP offering. Iranian governmental bodies, religious foundations, and private-sector enterprises issued five PPs between 1995 and 1997. PPs combine features of debt and equity in that they have specific terms ranging from22 to 5 years and set a minimum return, but may provide an actual return higher than the minimum if warranted by the ultimate profitability of the underlying investment.

Pricing and the method of distribution. Individuals and legal entities (incorporated bodies) may purchase participation bonds. Banks are not eligible purchasers at the primary distribution. PPs are sold at face value on a first-come, first-served basis.

Repurchases. After sale, a purchaser may resell a PP to the agent bank at face value plus accrued interest. The bank is expected to resell the bond at face value, less accrued interest, to the public on demand. No fee is changed for these secondary-market transactions.

Rates of return. The minimum return so far has been set by the credit committee[5]. As determined by the trustee, a balloon payment is expected to be paid on maturity. To date, PPs have only paid the guaranteed minimum rate.

Source: "Monetary Operations and Government Debt Management Under Islamic Banking", V. Sundararajan, D. Martson, and Ghiath Shabsigh, in Macroeconomic Issues and Policies in the Middle East and North Africa, Edited by Zubair Iqbal, IMF, 2001, pp. 89-115.

Concerted efforts are also under way to establish an International Islamic Financial Market (IIFM). The Initiative was spearheaded by Bahrain Monetary Agency (BMA), the IDB, and the Malaysian Labuan Offshore Financial Supervisory Authority. The IIFM will have two connected bases for trading (Bahrain and Malaysia). It will also include a liquidity management center (LMC) to be established in Bahrain and a market management center (MMC) in Labuan (Malaysia). The IIFM is expected to be dollar based, and trading will be electronically made. IIFM will be useful in facilitating IFIs international transactions, including settling international payments, facilitating the mobilization of foreign capital, and providing dollar-based investment opportunities.

Accounting and regulatory frameworks that are appropriate for the operations of IFIs are essential to ensure transparency and disclosure of their operations and compliance to regulatory standards of capital adequacy, governance, and Sharia. It was with these considerations in mind that the establishment of an Islamic Financial Services Board (IFSB) was initiated. The IDB is playing a facilitating role in this regulatory scheme (see Box 3.7).

Box 3.7: IMF facilitates the establishment of Islamic Financial services Board

On April 21, the central bank governors of Bahrain, Indonesia, the Islamic Republic of Iran, Kuwait, Lebanon, Malaysia, Pakistan, Saudi Arabia, Sudan, and the United Arab Emirates and senior officials from the Islamic Development Bank and the Accounting and Auditing Organization of Islamic Financial Institutions agreed to create an organization to promote good regulatory and supervisory practices and uniform prudential standards for Islamic financial institutions. That decision follows extensive consultation, coordinated by the IMF, with the collaboration of the Islamic Development Bank and the Accounting and Auditing Organization of Islamic Financial Institutions.
During the IMF-World Bank Annual Meetings in Prague in September 2000, central bank governors and senior officials of Islamic financial institutions asked the IMFG to help them form a standard-setting body. In the ensuring consultative process, V. Sundararajan and David Marston of the IMF's Monetary and Exchange Affairs Department spearheaded a series of meetings with central bank governors, as well as several technical meetings that helped work out the details of the organization.

The Islamic Financial Services Board (IFSB) will be based in Kuala Lumpur, Malaysia, and will complement the efforts of the Accounting and Auditing Organization of Islamic Financial Institutions, which sets accounting and disclosure standards. The IFSB will maintain close ties with other bodies being set up to promote Islamic financial instruments and markets. To help strengthen and harmonize prudential standards, the IFSB will also

- Set and disseminate standards and core principles - as well as adapt existing international standards for supervision and regulation, consistent with the Sharia principles, for voluntary adoption by member countries.
- Serve as liaison for and promote cooperation with other standard setters in the areas of monetary and financial stability; and
- Promote good practices in risk m management in the industry through research, training, and technical assistance.

A steering committee that would oversee the establishment and inaugurated of the IFSR, has already been formed.

Source: IMF Survey, IMF, 2002 p.

3.4 External Factors Constraining Resource Mobilization in IDB Member Countries

3.4.1 Openness, terms of trade and resource constraints

Due to their dependence on primary commodity exports, some IDB member countries are exposed to wide price swings and to unfavorable fluctuations in export earnings. This external vulnerability has become a source of serious concern and, consequently, limited the IDB member countries' ability to achieve a sustainable poverty-reducing growth. This has raised a lot of challenges for the IDB member countries. One major challenge is the increasing globalization of the world economy, and its adverse effects, particularly on the poor countries. To minimize the negative effects of globalization and to integrate in the world trading systems, the challenge facing IDB member countries lies in opening their economies to international trade. Trade openness is expected to enhance growth by improving investment and production efficiencies, and facilitating greater access

to capital goods and technology. Yet, a more open economy is also more vulnerable to external events such as terms of trade or foreign demand shocks.

Openness is defined as the ratio of total trade to GDP. Data in Table 3.6 suggest, among others, that many IDB member countries are not sufficiently open to foreign trade. The average degree of openness of most of the IDB member countries is less than 70 per cent, indicating that a significant number of the IDB member countries are not yet benefiting from liberalization or pursuing an active trade policy. Clearly, member countries with large trade sector are more likely to earn foreign exchange for financing their development.

Enhancing participation in the global economy has been an important part of the member countries' effort for liberalizing their economy. If accompanied by appropriate policy and institutional reforms, liberalization will help countries, through incremental gains from developed countries that reduced their protection measures. This is because a reduction in world barriers to trade could accelerate growth and lead to a more rapid pace of job creation and poverty reduction in member countries. However, trade reforms will not only deepen that participation, but also improve both the hard and soft infrastructure of trade (i.e., ports and customs administration, insurance, and finance). Many IDB member countries are still lagging behind competitors in these key areas. For example, the low level of port efficiency leads to frequent delays and high operating and shipping costs in many member countries. Moreover, bottlenecks in domestic transport (to get to the port) or in customs administration to get inputs into and outputs out of the country, are a kind of an additional "tax", eroding further potential profit.

Many IDB member countries, particularly those that have launched a stabilization program based on free market principles and an outward orientation of economic policies, are faced with the challenges of capital account liberalization. For example, Turkey in the 1980s embarked a liberalization program, including capital account liberalization and the opening of the securities markets to foreign investors, in the context of its membership in the OECD.

Apart from inflation, terms of trade movements also affect saving. The so-called Harberger-Laursen-Meltzer effect suggests that terms of trade improvements tend to lead to an improvement in the trade balance and an increase in saving. The positive correlation between transitory terms of trade shocks and saving was confirmed by Svensson and Razin (1983), though the effects of a permanent terms of trade shock are found to be ambiguous.

In general, with the exception of few member countries, most of the IDB member countries experienced on average, an apparent deterioration in the terms of trade. However, for the IDB member countries as a whole, the terms of trade improved during the second half of the 1990s, mainly as a result of the rebound in prices of oil and some nonfuel primary commodities. Seemingly, the burden of the terms of trade loss has fallen disproportionately on the poorest member countries during the said period. In this context, member countries which are heavily dependent on commodities that are exposed to wide short-term swings of prices, are generally recognized to be subject to additional constraints in financing their

economic development. Fluctuations in export earnings result in variations in domestic income and savings and increase uncertainties about the prospects for economic growth.

3.4.2 Current account, foreign reserves and saving

Although IDB member countries' exports growth ranged between an average annual rate of nearly 22% (Albania) and -6% (Turkmenistan), only few member countries have seen their imports decline. This perhaps explains the nearly consistent current account deficits in the large majority of the IDB member countries. Specifically, during the 1990s, nearly two thirds of the IDB member countries recorded an average current account deficit with few countries experiencing deficits of more than 10 percent of GDP. In particular, these current account deficits ranged between 1 and 2 per cent of GDP for high income member countries; they were more than 6 per cent for both the middle and low income member countries. However, for IDB as whole, the current account turned into a surplus in 1999, largely driven by only a handful of member countries-Malaysia, Indonesia and Kuwait (which recorded sizable surpluses in the said year)- thus masking the deficits in many of the members' economies. Adverse turns in the terms of trade, and the difficulties in expanding exports, largely explain this unfavorable developments in the external environment external sector during the said period.

For a given current account balance, the levels of savings and investment can have implications for the sustainability of the external position. High savings and investment ratios can also act as a signal of creditworthiness to international investors. It is further believed that countries with high growth rates can sustain persistent current account deficits without increasing their external indebtedness relative to GDP. Intuitively, this may suggest that the IDB member countries' growth performance, by and large, was not high enough to sustain the current account deficits and/or to ward off against further external indebtedness.

The general insight is that the current account deficits were mainly excessive, particularly for LDMCs. The other concern is the source of such current account deficits, as foreign savings could be financing excessive consumption and unproductive investment. Moreover, the positive and moderately large coefficient of correlation between foreign savings and national savings (0.56) seems to suggest that foreign savings and national savings in the IDB member countries are mutually reinforcing.

Additionally, international reserves accruing to the IDB member countries as a whole followed an upward trend during the 1990s. In terms of months of import equivalents, they were quite in line with the level of the developing countries in general, slightly trending up from 4 months to 6 months. However, for individual member countries, most of them were on the low side (Table 3.6) as the average months of import equivalents for the 1990s varied between a minimum of less than one month (Cameroon) and a maximum of a little more than 13 months (Lebanon).

Indeed, low foreign reserves and persistent current account deficits can contribute to the accumulation of a high level of external indebtedness. In other words, the heavy reliance by many IDB member countries on foreign financing, especially bilateral and multilateral loans, has in fact, contributed to the build up of their sizable external debt which increased by 60 per cent during 1990s to reach US$577 billion in 1999.

3.4.3 External indebtedness, debt relief and resource constraints

One of the major external constraints faced by many IDB member countries, especially the LDMCs, is external financing in general, and the debt burden in particular. As can be seen from Table 3.7, IDB's total external debt grew nearly by 60 per cent from a level of US$361 billion in 1990 to nearly US$577 billion in 1999. More than half of this debt is owed by a handful of member countries. Actually, the total external debt of the LDMCs amounted to US$42 billion in 1999. The debt-to-GNI (gross national income) ratio rose sharply from 35 per cent in 1990 to 60 per cent in 1999. As a ratio of exports, the debt increased from 139 per cent in 1990 to 152 per cent in 1999. Table 3.12 shows that the annual average ratio of the present value of the external debt to exports ranges between a high of 292 per cent (Cameroon) and a low of 48 per cent (Malaysia).

The debt problem has emerged as one of the most difficult development challenges confronting many IDB member countries, particularly the LDMCs. The external debt burden has reached unsustainable levels whereby, large foreign debt and high interest rates, combined with adverse terms of trade have made debt service payments difficult to manage. In 1999, nearly two thirds of the IDB member countries were classified as either severely or moderately indebted. The debt service for the whole IDB member countries was absorbing nearly one fifth of their exports in 1999, and many of them were unable to service their debt without recourse to rescheduling or accumulating arrears.

Although the share of IDB member countries' debt in the total debt of the developing countries is low (nearly 23 per cent in 1999), its relative burden is quite high (6.8 per cent of GNI compared to 6.3 per cent for developing countries in 1999). In sum, the last decade has witnessed an increase in the level of the IDB member countries debt. This debt is characterized by being predominantly long-term, mostly owed to multilateral and bilateral creditors, growing due to the accumulation of interest and principal arrears (usually capitalized through the Paris and London clubs). Debt burden indicators also show that the external debt is extremely heavy compared to the capacity of member countries' economies, in particular their export sectors.

Table 3.6: Foreign Trade Factors and Saving (1990-1999 Averages)

Country	Gross Dom. Saving Ratio	GDP Growth Rate	Current Account % of GDP	Monthly Imports	Export Growth Rates	Import Growth Rate	Terms of Trade (1990=100)	Openness (% of GDP)
HIC								
Algeria	30.2	1.3	3.7	5.4	2.9	-2.4	94.8	50.8
Bahrain	37.2	3.9	5.2	..	..	..	..	194.6
Gabon	41.7	2.8	1.3	0.7	2.7	-0.2	86.9	87.6
Iran	26.7	4.8	1.3	..	3.8	-3.2	83.2	40.7
Kuwait	10.8	10	-10.4	4.5	..	..	98.4	98.6
Malaysia	40.6	7.2	-1.6	3.9	12.7	12.5	100.0	178.1
Saudi	29.8	2.8	-7.8	3.0	..	..	78.7	76
Tunisia	23.9	5.1	-4.2	2.0	4.9	4.4	98.8	89.1
Turkey	20.4	3.8	-0.8	3.6	9.4	12.2	101.6	41.8
UAE	36.2	3.8	..	..	..	..	78.5	119.6
MIC								
Indonesia	32.3	4.8	-1.1	3.7	5.1	6.8	98.1	57.1
Jordan	4.6	4.9	-5.5	4.4	3.6	6.9	112.8	126.2
Kazakhstan	18.2	-5.3	-3.0	2.8	5.6	-1.8	..	82.9
Lebanon	-31.1	11.5	-22.4	13.4	13.1	12.2	103.4	81.1
Morocco	17.1	2.6	-1.3	4.3	6.2	7.3	98.3	58.6
Syrian	16.3	6.1	1.9	..	6.9	2.8	76.8	67.4
Turkmenist	18.6	-3.9	-11.7	7.0	-6.0	1.3	..	102
LIC								
Albania	-14.4	0.4	-5.7	3.9	21.6	31.9	..	53.5
Azerbaijan	12	-7.4	-14.8	1.3	16.3	14.9	..	80.3
Bangladesh	13.4	4.9	-1.7	4.0	15.0	11.5	95.9	25.7
Benin	4	4.5	-4.9	3.7	6.3	7.2	83.2	45.3
Burkina	8.5	3.8	-5.4	5.6	6.0	5.3	99.7	39.4
Cameroon	19	0.4	-2.8	0.1	2.3	4.6	97.4	42.4
Chad	-1.4	2.1	-5.1	2.7	2.4	-0.8	90.1	45.8
Comoros	-3.7	0.1	-7.4	5.3	10.4	-0.2	75.6	62.7
Djibouti	-10.5	-2.1	-10.0	2.7			..	113.1
Egypt	13.4	4.5	1.7	9.2	3.9	3.3	114.2	50.8
Gambia	4.9	3.3	-1.9	4.1	1.0	1.7	99.8	121.8
Guinea	14.2	4	-5.5	1.4	4.2	1.6	82.3	47.1
Guinea-Bissau	1.2	1.2	-21.1	2.6	25.9	-0.4	80.7	51.1
Kyrgyz	4.8	-3.4	-11.4	1.8	-0.5	-7.2	..	82
Maldives	25.2	7.7	-7.1	2.0	..	..	..	130.5
Mali	7.7	3.2	-8.8	4.2	10.2	3.5	90.3	56.1
Mozambiqu	-6.6	5.6	-15.9	3.1	14.6	6.4	81.1	50.5
Niger	2.7	1.9	-8.3	2.7	2.7	-3.9	91.1	38.6
Oman	28.2	6.2	-4.5	3.5	..	..	85.0	87.9
Pakistan	12.1	4	-4.0	1.6	3.7	2.6	103.9	38.5
Senegal	10.1	3.3	-5.5	1.4	2.4	1.7	89.7	66.1
Sierra	1.8	-4.1	-6.4	1.6	-5.0	-0.8	98.4	45.5
Suriname	21.3	3.1	2.2	2.1	5.0	23.3	90.8	38.9
Tajikistan	15.1	1.6	-2.5	0.7	-0.7	-5.3	..	125.8
Togo	7.3	1.7	-8.0	2.9	-1.5	0.1	91.9	69.8
Uganda	3.8	6.9	-10.1	3.1	14.5	7.7	95.4	31.2
Yemen	7.2	3.1	-3.4	2.6	9.9	..	..	65.5

Source: WDI, World Bank, 2002

Debt sustainability is crucial for many IDB member countries, particularly the LMDCs. The HIPC Initiative launched in 1996 to relieve developing countries of their high debt burdens has entitled a number of member countries for debt relief. At the end 2000, Benin, Burkina Faso, Cameroon, Guinea Bissau, Mali, Mauritania, Mozambique, Senegal, and Uganda became eligible for debt relief by reaching their decision points. However, with very few exceptions, the international debt relief efforts have not adequately contributed to relaxing financial constraints as many indebted member countries feel that not enough resources were freed to be directed towards poverty reduction. There is also a fear that the debt relief may detract from the official development assistance (ODA).

Another major constraining factor was capital flight. In many LDMCs, capital flight acts as a compounding factor to the already severe debt problem. In most cases, capital outflows are triggered by the low quality of the investment climate in poor countries. Political instability, bad governance, macroeconomic instability, uncertainty over property rights, high tax rates, weak governmental institutions, financial repression, and unnecessary constraints on private sector economic activity are likely to encourage capital outflows by limiting the opportunities for profitable domestic investment and increasing the risk of capital losses.

Some economists have argued that there is no causal link between external debt and capital flight, while others have found evidence for such a relationship (Ajayi, 1997). It was found that high inflation, budget deficits, and low interest rates were associated with increased capital flight. In poor countries with better than average economic policies, the stock of total outflows totaled only 6 per cent of GDP, compared with 30 per cent of GDP in countries with worse than average policies (World Bank, 2002).

Table 3.7: External Financial Resources and Saving (1990-1999 Averages)

Country	Gross Dom. Saving Ratio	GDP Growth Rates	Gross Private Capital Flows (%GDP)	ODAOA ($Million)	Long Term Debt ($Million)	Short-Term Debt %Total External Debt	Present Value of the Total Debt % Exports	Debt Service % of Exports
HIC								
Algeria	30.2	1.3	1.3	312	27609	1.9	206	50
Bahrain	37.2	3.9	285	66	..	..	..	..
Gabon	41.7	2.8	12.5	103	3479	13.8	..	..
Iran	26.7	4.8	1.6	156	7954	50.9	..	..
Kuwait	10.8	10	17	4	..	..	..	..
Malaysia	40.6	7.2	7.6	87	25062	20.6	48	..
Saudi Arabia	29.8	2.8	9.8	28	..	..	..	..
Tunisia	23.9	5.1	3.5	225	8568	10.9	..	..
Turkey	20.4	3.8	3.7	421	56851	21.3	185	27.3
UAE	36.2	3.8	..	-1	..	..	..	..
MIC								
Indonesia	32.3	4.8	2	1613	88979	18.9	255	..
Jordan	4.6	4.9	5.0	525	7122	10.6	..	..
Kazakhstan	18.2	-5.3	3.8	96	2757	9.7	89	6.3
Lebanon	-31.1	11.5	..	199	2033	55.6	..	..
Morocco	17.1	2.6	1.6	738	21130	1.2	135	29.9
Syrian	16.3	6.1	6.1	341	16211	20.1	..	..
Turkmenistan	18.6	-3.9	2.4	19	879	18.7	..	..
LIC								
Albania	-14.4	0.4	2.7	247	416	41.7	..	..
Azerbaijan	12	-7.4	4.5	101	259	2.9	..	..
Bangladesh	13.4	4.9	0.4	1490	14486	1.3	..	..
Benin	4	4.5	5.9	256	1391	4.2	148	7
Burkina Faso	8.5	3.8	1.3	415	1068	5.4	..	11
Cameroon	19	0.4	6.8	516	7294	12.7	292	..
Chad	-1.4	2.1	2.3	237	790	3.3	..	..
Comoros	-3.7	0.1	1.3	41	180	6.5	278	7
Djibouti	-10.5	-2.1		..				
Egypt	13.4	4.5	2.3	2887	28493	9.6	127	14
Gambia	4.9	3.3	0.9	66	376	5	103	13
Guinea	14.2	4	1.1	358	2781	6.7	..	..
Guinea-Bissau	1.2	1.2	8.4	118	768	8.7	..	32
Kyrgyz	4.8	-3.4	1.7	188	746	1.7	228	10.4
Maldives	25.2	7.7	4.3	32	132	5.6	..	..
Mali	7.7	3.2	2.2	433	2672	3.6	193	12.9
Mozambique	-6.6	5.6	0.7	997	6046	4.3	..	..
Niger	2.7	1.9	2.2	319	1436	4.9	362	18.9
Oman	28.2	6.2	..	52	2400	23.1	..	..
Pakistan	12.1	4	1.3	1021	23640	10.6	..	26.6
Senegal	10.1	3.3	2.7	596	3112	8.1	169	17.1
Sierra Leone	1.8	-4.1	1.4	147	810	23.3	..	..
Suriname	21.3	3.1	7.7	68	..	..	..	..
Tajikistan	15.1	1.6	..	73	565	5.7	..	3.1
Togo	7.3	1.7	2	158	1198	7.6	216	..
Uganda	3.8	6.9	0.8	680	2901	3.8	225	40.4
Yemen	7.2	3.1	6.7	298	4837	11.9	91	4.5

Source: WDI, World Bank, 2002.

Table 3.8 shows that during the 1980-1993 period, the IDB member countries with the largest cumulative capital flight were Sudan ($199 million), Niger ($155 million); and Guinea-Bissau ($69 million). In addition, capital flight as a ratio of GNP is high in Sudan (1.34) and Guinea-Bissau (1.15). Equally, as a proportion of exports, it is high for both countries (17.7 and 13.5 respectively); and as a ratio of the external debt, Sudan scores high (0.61), followed by Uganda (0.44), and Guinea-Bissau (0.42).

Table 3.8: IMF Capital Flight Estimates for Selected Member Countries (1980-1993)* (In millions of US dollars)

	80	81	82	83	84	85	86	87	88	89	90	91	92	93	Sum	A1	A2	A3
Guinea-Bissau	..	..	9	5	13	10	4	8	-4	12	2	16	-22	16	69	1.15	0.42	13.5
Mali	25	-27	-13	7	-1	18	16	-2	2	2	-1	-29	23	-23	-3	0.40	0.36	2.65
Mauritania	32	7	-5	-11	9	12	16	85	25	7	-143	-213	-226	-144	-546	0.23	0.11	0.55
Mozambique	30	70	42	-9	-26	13	29	-40	-85	-57	-66	4	-32	..	-127	0.32	0.08	2.45
Niger	35	19	7	9	-14	-27	66	15	-43	4	25	40	3	16	1554	0.20	0.20	1.05
Sierra Leone	22	46	-85	31	20	17	-20	20	26	-47	-27	-1	..	..	2	0.56	0.29	2.52
Somalia	-2	-19	-75	4	-23	-15	-19	-40	-22	1	..	..	..	..	-210	..	..	..
Sudan	-58	-15	-13	-145	2	125	89	195	-3	160	-9	-98	-31	..	199	1.34	0.61	17.7
Uganda	65	38	25	37	-25	12	-105	-26	-155	38	-10	-1	-11	-43	-161	0.50	0.44	6.35

Notes: A1=Average Capital Flight/GNP; A2= Average Capital Flight/External Debt; A3= Average Capital Flight/Exports. Values are as of 1991. *Extracted from S. Ibi Ajayi: An Analysis of External Debt and Capital Flight in the Severely Indebted Low Income Countries in Sub-Saharan Africa, IMF WP/97/68, June 1997.

However, owing primarily to the policies under way and the episodic events in their economies, capital flight was reversed in Uganda (since 1986), and Mauritania (since 1990). Just as poor investment climate induces capital flight, its improvement can encourage repatriation. Therefore, it is crucial for member countries, particularly those with history of capital flight, to devise policies that deter further capital flight.

3.5 Institutional Challenges for Resource Mobilization in IDB Member Countries

Empirical research on growth indicated that, a country's growth rate generally depends on endowments, preferences, institutions, macroeconomic stability, an outward orientation, and financial market development [Barro, (1990, 1991), Grossman and Helpman (1992), Romer (1986), Locus, (1988)].

The institutional quality is widely recognized as a crucial requirement for effective resource mobilization and sustainable growth. For example, it is widely believed that good policies and strong governance, along with sound institutions, are key to improving aid effectiveness and using private flows productively (World Bank, 2002).

Despite some efforts towards both structural and institutional reforms in many IDB member countries, the existing institutional frameworks (e.g., corruption, poor public services, lack of transparency, and poor contract enforcement etc.) largely explain why some IDB member countries, have failed to attract or mobilize enough resources to promote poverty-reducing growth.

To analyze the institutional quality in the IDB member countries during 1990s, one may focus on key areas such as political stability, governance, accountability, and the rule of law. Data on institutional effectiveness are extracted from Composite Indicator Dataset of the World Bank[6].

The governance indicators reflect the statistical compilation of perceptions of the quality of governance of a large number of survey respondents in industrial and developing countries, as well as non-governmental organizations, commercial risk rating agencies, and think-tanks during 2000 and 2001[7]. The six governance indicators in table 3.10 are measured in units ranging from about -2.5 to 2.5, with higher values corresponding to better governance outcomes. The values of these indicators are based on data referring to 2000-2001.

Government effectiveness measures bureaucratic delays, competence of officials, the quality of public service delivery and the independence of the civil service from political pressures. This group of indicators covers the elements needed for the government to design and implement good policies. Based on performers government effectiveness and control of corruption, Tunisia was the best (1.30 and 0.86 respectively).

The adverse impact of corruption on economic performance has been documented in research (Maoro, (1995) Keefer and Knack, (1995) and Wei, (1997) among others.). Corruption has been identified to be mostly a symptom of underlying distortions and weak economic institutions. The impact of corruption on economic performance has raised concerns among bilateral and multilateral aid agencies. Yet, there remains a significant degree of ambivalence among policy makers about the real impact of corruption on the economy (Campos et. al., 1999).

Meanwhile, structural and institutional reforms, including the rationalization of state functions, reliance on market-based pricing, and the establishment of a sound regulatory environment are more important than corruption per se in explaining differences in economic performance as reflected in growth, inflation, the fiscal balance, and both domestic and external resource mobilization (Abed and Davoodi, July 2000). It is even argued that structural reform is an important factor in lowering corruption levels. One implication of this analysis would be to stress the need for member countries to adopt consistent structural reforms.

Regulatory burden includes the numbers of regulations within a market, the number of markets that are regulated, competition policy measures, and price controls. Generally, it happens that there is an oversupply of regulations whose interpretation often leads to confusion and abuse on the part of the bureaucrats who administer them (Tanzi, 2000).

Rule of law captures the extent of crime, property rights violations, tax evasion, and the legal system's effectiveness. It also indicates the enforceability of contracts and the predictability of rules. A legal structure that clearly defines, among other things, property rights and enforces contracts provides the foundation for a free economy. With the exception of Brunei which recorded the highest score (1.29), and Kuwait (1.10), the majority of member countries scored very low with respect to the rule of law.

The political instability measure is primarily concerned with the probability of violent shifts in political power rather than constitutionally sanctioned shifts in policy stance. In terms of political stability, many of the IDB member countries are scoring poorly. This suggests that political instability, ranging from rapid government turnover to socio-political unrest, is harmful to economic growth and hence to saving and resource mobilization. In some IDB member countries, it has even interrupted financial flows (Elbadawi, 1999). As widely recognized, any deterioration of the political climate of countries is likely to worsen economic growth.

Although there is an emerging consensus on the importance of the institutional reforms in mitigating resource constraints, experiences from the IDB member countries suggest that sequencing reforms and at times adapting cultural norms and orientation of these societies may provide innovative mechanisms to relax such constraints, as discussed in chapter four.

End notes of Chapter III

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[1] The ratio of government expenditure to GDP is generally high for the majority of the member countries, revealing a substantial presence of the government in the economy. However, according to the Heritage Foundation grading scale, on average, most member countries fall between low and moderate levels of government intervention in the economy (11 to 35 per cent of GDP (Wall Street Journal, Economic Freedom, 1999).

[2] Chapter offers a detailed account of the experience of Islamic financial institutions in relaxing resource constraints in the Sudanese economy.

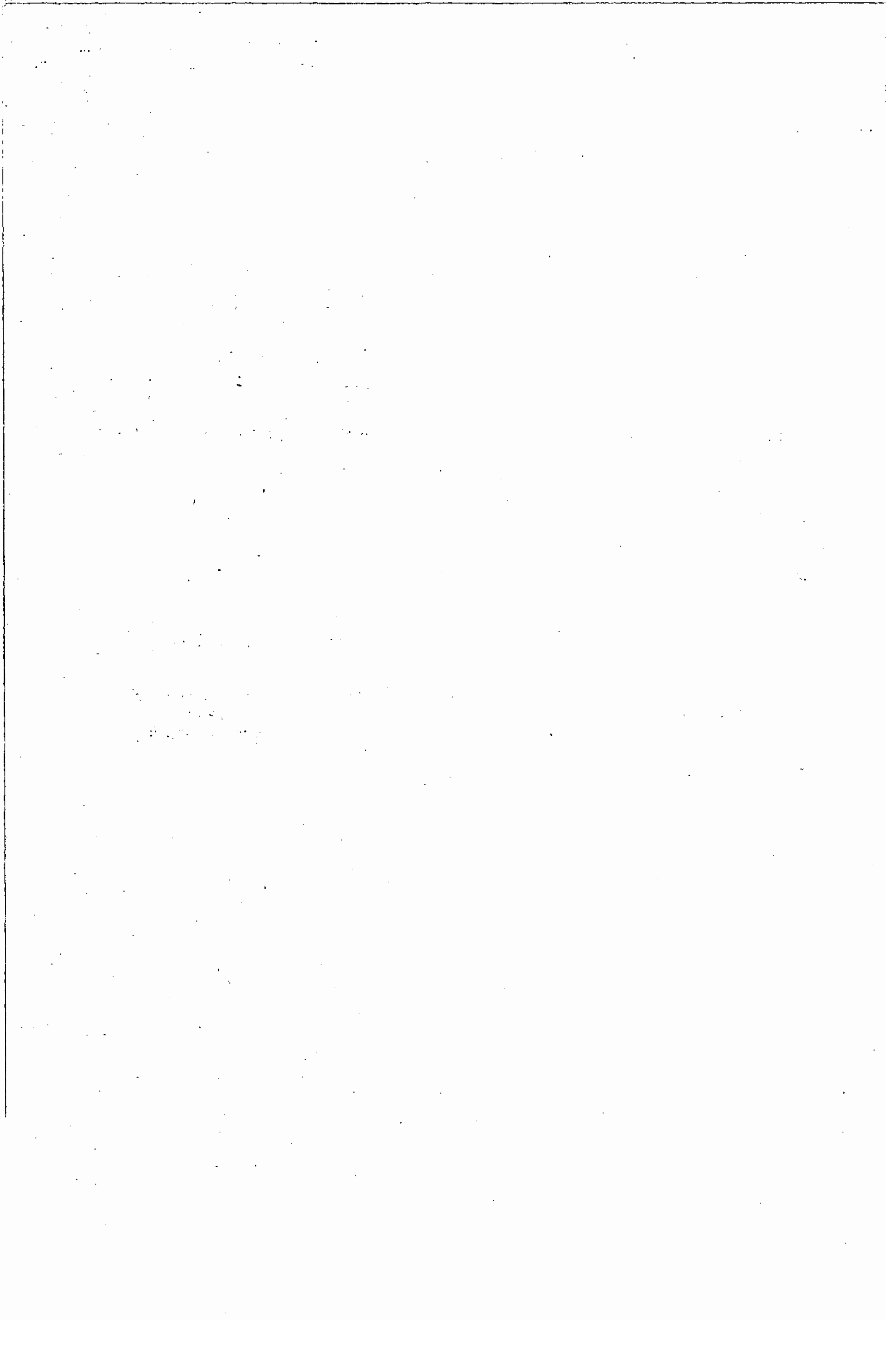
[3] For more discussion of Islamic financial instruments, see Kazarian (1983) and Iqbal and Mirakhor (1987).

[4] Presumably, the borrower deducts fees and other payments from projected financial flows to reward his own entrepreneurship and management acumen.

[5] It has been kept above bank deposits with similar terms to ensure marketability and to compensate for a 5 percent tax applied to the return from PPs, but this is not applied to earnings from bank deposits.

[6] This composite indicators of six dimensions of governance are constructed using an unobserved components methodology described in detail in (Kaufmann et al., 1999a, 1999b, 2002).

[7] Details on the concepts measured by each indicator, its components, and the interpretation of the point estimates can be found in the research paper by Kaufmann, Kraay and Zoido-Lobaton (2001). All indicators are subject to a margin of error. Papers are available at www.worldbank.org/wbi/governance/wp-bovernance.htm.



IV. SELECTED LDMCs EXPERIENCE IN COPING WITH RESOURCE CONSTRAINTS FOR FINANCING DEVELOPMENT

4.1 The Role of Islamic Finance in Relaxing Financial Constraints and alleviating poverty in Sudan

4.1.4 Introduction

As a typical less developed country, Sudan suffers from inadequacy of financial resources to generate growth and reduce poverty. On its endeavor for development, the country had depended heavily on foreign credits and aids. However, the 1990s period was characterized by heavy foreign debt and suspension of grants and credit from most of the international financial institutions. This difficult situation created a challenge that forced the authorities to depend on local financial resources to mitigate resource constraints, promote growth and alleviate poverty.

This section will focus on the innovative approaches used by the Sudanese Islamic Financial Institutions (IFI) to mobilize domestic savings to finance small and medium-sized enterprises and, hence help in the poverty alleviation efforts currently under way in Sudan.

4.1.4 Islamic banking and monetary policy 1990-2000:

The Islamization of all financial institutions in Sudan was first introduced in 1984, but not until the beginning of the 1990s that serious efforts have been taken to develop tools and modes of Islamic finance that can take a lead in mitigating constraints to promote growth and alleviate poverty.

The Central Bank took serious efforts to deepen the real practice of Islamic banking. Those efforts were clear in the issue of the Banking law in 1991, the establishment of the High Sharia Supervisory Board, as well as the establishment of Khartoum Stock exchange (KSE) market and Banks Deposit Security Fund and Exchange Bureau.

During the period that started in the early nineties, serious efforts were taken to deepen practical conversion to Islamic banking as previously mentioned. Consequently the credit policy was renamed "the financing policy" an authentication for Islamic banking being based on Musharaka and not on credit basis.

The financing policy has much relied on Musharaka and Murabaha Modes for sectoral directions of finance by giving preferential treatment for the named priority sectors. Mudaraba mode was allowed only for financing exports and small producers and professionals and handcrafts (restricted Mudaraba), and it is not allowed for local trade finance. The financing policy specifies the financing ratios for priority sectors. Specifically, the agricultural sector and small industries and handcrafts. The policy also specified the operations that banks are not allowed to finance as well.

The central bank also launched the banking conformity program in August 1993. The program aimed at restructuring the banks in order to create strong legally and financially sound banking institutions that can compete both internally and internationally. Within this program, the Bank of Sudan adopted the Basle Commission Capital Sufficiency Standards with a view to incorporate those measures into the Islamic Banking System in the Sudan.

Rural sector finance has been introduced during this period as well. The commercial banks were directed to use not less than 50% of their deposits in the same area so as to promote rural development and to reduce trade financing.

The most important tool of liquidity control in an Islamic banking system has been innovated in Sudan by the introduction of the Central Bank Musharaka certificates (CMC) in June 1998 and the Government Musharaka Certificates (GMC) in 1998 as well (Box 4.1).

Box 4.1. Securitization of Islamic Instruments in Sudan

The first generation of securities called The Central Bank of Sudan Musharaka certificates (CMC), were first issued in June 1998. The CMC represents the share of the holder in a special fund consisting of the equity ownership of both the Bank of Sudan and the Ministry of Finance in the banking sector. The CMC has a face value specified in the certificate and a fair market value to be announced monthly to represent dividends and capital gains and/or losses. The exchange value of CMC is negotiable and the certificate has no maturity. While trading of CMC is mostly done through auction, some transactions are completed outside the auction. CMC thus represents a highly liquid investment asset for commercial banks and financial institutions and at the same time a mechanism of liquidity control by the central bank. The issuance of CMC requires the establishment of an Open Market Operations Fund (OMOF) that would hold the shares in commercial banks that the government and the central bank owns that forms the base for issuing the CMCs. The face value of the certificate is one million Sudanese Dinar (SD) while the fair market value is the CMC fund's equities plus reevaluation of net foreign assets and liabilities of these commercial banks constituting the fund. The fair value for the banks' equity was SD3,94 billion in 30/4/1998 and thus 3940 certificates were issued. The CMC holder doesn't own shares in the equity of the commercial banks but he shares gains and losses of the equities owned by the Central Bank and Ministry of Finance in those commercial banks. The Khartoum Stock Exchange (KSE) provides a secondary market for CMC.

Another group of certificates is the Government Masharaka certificates (GMC). GMC are securities issued against certain percentage of government ownership in profitable ventures and enterprises. The GMC are based on Masharaka contracts between the government and investors in gains and losses in a pool of assets, and are thus securitization of assets as described in the case of CMC. The GMC are fixed term securities, issued in fully registered form, transferable and fully negotiable. Since GMC are listed in KSE market, they have a well-developed secondary market and are thus, highly liquid.

GMC's were first issued in May 1999 to mobilize national savings and encourage investment. The GMC certificates proved to be highly profitable for investors as the fair value is based on gains from highly profitable enterprises. The achieved average profit was 30%.

GMC furnish the monetary authorities with an Islamic monetary instrument for the management and execution of monetary policy and enable the government to finance its budget though non-inflationary instrument. Auctioning of GMC provides an Islamic alternative tool for OMO to control liquidity.

The issuing of GMC certificates with small face value and shorter maturity, of three to six months, have succeeded in attracting small savers to invest in these certificates. Further their acceptance as guarantee for financing and in transactions settlements rendered them viable Islamic securities. Hence, issuing small denomination GMC is certainly a first step towards the development of an Islamic Money Market.

Source: Out-sourced study on Islamic financing in Sudan 2002

4.1.3 Effects of financing policy (1990-2000)

The clarity and specifications of the monetary and financial policy objectives have helped in the spread of banking services to various part of the country, specially the rural areas and further established the Islamic banking fundamentals. The stability of the policy during this period also helped banks to increase resources to around 50% of the money supply (the narrow money). However, this still considered low because of the low returns on investment deposits and the no reward on current deposits. On the other side, the total amount of banks' advances increased from SD1,766 million in 1990 to SD14,515 in 1995 and lately to SD79,224 million in 2000.

Deposits:

Table 4.1.1 shows the annual increase in total banks' deposits, specially in the first half of the 1990s when a number of new banks and new branches were established as the result of the encouraging policy adopted thy by the Bank of Sudan. Table 4.1.2 shows the type of deposits and the percentage of savings and investment to the total deposits. The increase in savings and investment deposits shown in Table 4.1.1, reflects the public confidence in Islamic banking operations and the serious efforts taken by the monetary authorities. Yet, the share of current deposits is considered high for Islamic Banks.

Table 4.1.1: Sudan's Banks' Deposits & Advances (1990-2000)
(Million Sudanese Dinars)

Year	Deposits	Advances
1990	-	1766.7
1991	2985.9	1402.6
1992	9444.5	3310.7
1993	16734	5272.5
1994	23435.5	10073
1995	41642	14515
1996	67792	33948
1997	96754.4	41556
1998	122112	47383
1999	145519	48732
2000	197224	79224

Source: Bank of Sudan annual reports.

Table 4.1.2: Types of deposits (1984-2000)

(Million Dinars)

Year	Current Accounts	Investment & Saving accounts	Total deposits	Share of I&S %
1983	115.7	62.43	178.13	35
1984	138.3	68.04	206.34	33
1985	275.47	86.78	36225	24
1986	329.98	183.71	513.69	36
1987	475.34	241.43	716.77	34
1988	584.31	275.62	859.93	32
1989	957.89	353.78	1311.67	27
1991*	2043.09	942.8	2988.89	32
1992	5066.17	4378.27	9444.54	46
1993	6414.5	10319.5	16734	62
1994	9847.4	13588.1	23435.5	58
1995	29325	12317	41642	30
1996	51442	16350	67792	24
1997	65673	31081.4	96754.4	32
1998	83582	38530	122112	32
1999	59295	86224	145519	59
2000	87203	110021	197224	56

Source: Bank of Sudan annual reports. *Data for 1990 is not available.

The figures in the table give the amount of deposits as on 31st of December each year, this justifies some of the fluctuations in the share of investment & saving accounts in the total, yet, it reflects the continuous increase in investment deposits.

Advances:

The continuous increase in banks' advances reflects the noticed increase in Islamic banks' ability to mobilize domestic resources. As can be seen from Table 4.1.2, the average annual increase in total advances was 63% during the period 1991-2000. This could as also be an indication of the success of the financial policies and procedures adopted to activate the banks' role in financing development. The sectoral distribution of banks' advances is shown in Table 4.1.3 below.

The share of the agricultural sector in banks' advances showed the largest increase, from below 5% before 1990 to an average share of 30% during the 1990s. The agricultural sector is considered the leading sector in the economy and all national policies were directed to develop agricultural products, including animal resources. The financing policy has specified a minimum share of 50% for agriculture. The exports sector comes next, taking about 20% of banks' advances. In fact, until 1998, most of Sudan's' exports were agricultural crops. The industrial sector received, on average, about 16% of banks' advances and is considered among the priority sectors. The share of local trade sector has very much been reduced to give more to the producing sectors.

Table 4.1.3: Sectoral Distribution of Banks Advances
(Million Dinars)

	Agriculture	Industry	Exports	Imports	Local trade	Others	Total
1991	373 26.7%	277 19.7%	257 18.3%	28 2%	193 13.7%	275 19.6%	1403 100%
1992	1125 34%	455 13.8%	570 17.2%	37 101%	383 11.6%	740 22.3%	3310 100%
1993	1865 35.9%	827 15.7%	1154 21.9%	43 0.9%	318 6%	1065 20%	5272 100%
1994	2946 29.3%	1840 18.3%	2236 22.2%	105 1%	566 5.6%	2379 23.6%	10072 100%
1995	3579 24.7%	2618 18%	3947 27.2%	1227 8.5%	419 2.9%	2726 18.7%	14516 100%
1996	8997 26.5%	6385 18.8%	6643 19.6%	1705 5%	1216 3.6%	9003 26.5%	33949 100%
1997	12522 301%	7284 17.5%	8387 20.2%	858 2.1%	1738 4.2	10767 25.9%	41556 100%
1998	15763 33.3%	8908 18.8%	8114 17.1%	325 0.7%	2038 4.3%	12235 25.8%	47383 100%
1999	14833 30.4%	7184 14.7%	8359 17.2%	1519 3.1%	2816 5.8%	14021 28.8%	48732 100%
2000	17807 22.5%	8343 10.5%	16839 22.3%	1125 1.4%	8243 10.4%	26867 33.8%	79224 100%

Source: Bank of Sudan annual reports.

All banks' advances were issued through Islamic modes of finance. The average shares of these modes during the nineties were 41.4% Murabaha, 36.9% Musharaka, and 3.9%, 4.2% and 13.6% for Mudaraba, Salam and others respectively. The high rating for Murabaha was justifiable in the early years of conversion to Islamic banking for its ease and low risk. Currently, the Comprehensive Banking Policy directs banks to reduce Murabaha financing to no more than 30% of total finance and Murabaha margins are being reduced concurrently. Banks are persuaded to use Musharaka and to take more direct role in production and development financing.

4.1.4 The Sudanese Banking efforts and Experience in Mitigating Resource Constraints and Alleviating Poverty

The beginning of the 1990s witnessed the adoption of economic liberalization and elimination of government subsides for many essential commodities. These developments created the need for social safety nets and poverty alleviating programs that were later incorporated in the National Comprehensive Strategy (1992-2000). A steering committee for the strategic program of poverty alleviation was formed within the Ministry of Finance. The committee is now working on designing a poverty alleviation strategy for the next twenty-five years (2002-2027).

The main objectives of the poverty alleviation strategy were identified as follows:

- Promoting poverty-reducing growth through increasing the national income and mobilizing more resources for social funds.
- Reducing unemployment through labor-intensive programs to improve skills.
- Making funds available to finance small-scale producers, poor farmers, and tie the financing with training and literacy programs.
- Focusing on rural development programs to increase the productivity of agriculture and animal production.
- Conflict resolution, especially the civil war in the south, should be given priority in order to attain social and political stability.
- Increasing investment in health care to reduce the effects of infectious diseases.

Moreover, the strategy also called for providing basic necessities such as clean water, education, medical care and more jobs for women. The strategy aims at reducing the ratio of population below poverty line to no more than 10% by 2005 and 5% by 2010, and to reduce the ratio of those living bellow sufficiency to 5 – 10% by 2020.

To ensure that banks play an important role in reducing poverty, the financing policy specified certain sectors to be given priority in financing. These sectors included small and handicrafts industries, medium enterprises, and rural farming. In 1998, banks were required to direct 7% of their financing to the small industries and productive families. Moreover, less margins on Murabaha and easier guarantee requirements on financing were specified to that section of the economy.

The remaining part of this section will deal with selected banks efforts in reducing poverty as part of the rational efforts in this regard.

- Faisal Islamic Bank Sudan (FIBS):

Faisal Islamic bank was established in 1977 as the first Sudanese Islamic bank. Since its inception, development financing was one of its basic activities. Table 4.1.4 below shows the sectoral distribution of Faisal Islamic bank advances.

Table 4.1.4: Faisal Islamic Bank Advances by Sector

(Million Dinars)

	1980	1985	1990	1995	2000
Local Trade	2,2	6,2	19,8	167,4	318,5
Foreign trade	3,4	1,3	5,9	311,7	988,8
Industry of handcrafts	0,1	1,5	5,5	13,9	490,5
Agriculture	0,0	0,6	6,2	72,7	513,0
Services	0,0	0,4	2,6	11,5	1051,2
Total	5,7	10,0	39,8	577,2	3362,0

Source: the Faisal Islamic Bank, Investment Department

The bank's role in financing rural development is reflected by the increase in the share of the agricultural sector, handcrafts and related industries. FIBS was a pioneer in establishing a branch specifically for handicrafts and small industries financing. The branch, which was established in 1981, has its own procedures in financing small-scale producers using the Islamic modes such as Murabaha and Musharaka. Personal and collective guarantees were taken while small producers were exempted from paying the first installment in advance as customary in Murabaha financing. Moreover, the branch provided technical assistance and training for customers as well.

FIBS' performance and profitability from agriculture and small-scale industries can be seen from the actual rate of return on investments achieved in these sectors.

The actual rate of return on investment is obtained by dividing actual return on investment by the bank advance. It is clear from Table 4.1.5 that the agricultural and the industry and handcrafts sectors achieved high rates of return on investment during the period 1996-2000, amounting, on average, to 20% and 16% respectively, surpassing the average rate for all sectors combined (12%). The expected rates of return on investment in these sectors were also high for the same period (13% and 18%), reflecting low investment risks in the small industries.

Table 4.1.5: Actual rate of return on investment by sector in Faisal Islamic Bank (%)

Sector	1996	1997	1998	1999	2000	Average
Foreign Trade	14	5	22	18	6	13
Local Trade	7	10	7	5	8	7
Industry & handicrafts	13	12	19	21	13	16
Agriculture	37	11	23	16	15	20
Services	3	5	8	10	8	7
Total	14	7	17	11	9	12

Source: Faisal Islamic Bank, Investment department

In conclusion, FIBS has given much priority to development finance by directing the biggest share of its credit ceiling to the productive sectors, namely agriculture and industry. Most of the industries financed, such as edible oil and livestock exports, were agro-based. The handcrafts industries finances were also focusing on traditional agricultural machinery and its spare parts. The bank's modes of finance, especially Musharaka and Salam, have helped to reduce investment risk in agriculture by sharing these risks with the farmers.

- **The Sudanese Islamic Bank (SIB):**

The Sudanese Islamic bank was established in 1983 as a joint venture with Sudanese and foreign capital. The bank put more emphasis on social development projects and has chosen small farmers projects as one of its main targets. To promote rural development, the bank established a rural development department at its head office and employed agriculturists and economists with high

qualification. A number of small rural sub-branches were opened in rural areas. The mode used in financing small farmers was mainly Musharaka. In the Musharaka contract, SIB committed itself to:

i) Providing all agricultural inputs and selling them to the farmers at cost prices, ii) Providing working capital, iii) Providing agricultural services, and iv) Providing help in storage and marketing. On the other hand, the farmer's commitments include: i) Providing land, labor and part of the working capital, and ii) Participating in the administration of the project jointly with the bank.

Under this Musharaka system, the profit will be divided between the farmer and the bank.. In case of a loss, the farmer will lose his effort and land earnings and would not be indebted to the bank. The SIB bank also used Musharaka to finance small producers and productive families engaged in poultry production and simple machinery and tools manufacturing projects.

In compliance with its developmental drive, the bank established a special credit office (sub-branch) to offer finance and technical assistance to poor productive women in Omdurman and to Housewives Cooperative Societies. The most important feature of this credit office was the introduction of a new banking practice of the group-collateral concept. Every five women could form a group depending on mutual selection, and the group would offer a collective guarantee when individual members apply for loans. In case of default, the whole group will be responsible for repayment. The role played by SIB in promoting social development and alleviating poverty depend less on the amount of advances offered to the poor farmers, families and handcrafts, than on the new approach used to remove the barrier between small producers and the banks. The Musharaka mode used has helped the bank to attract technical and financial assistance from the international organizations working on the field of rural development such as the Dutch Aid Program, the Accord and Fredrich Ibert Agency and UNDP.

- **The Savings and Social Development Bank (SSDB)**

The SSDB was established in 1974 as the first rural bank in Sudan. The main objectives of establishing the bank were to attract small deposits, to spread the savings culture among the rural population, to use these deposits to finance small rural projects, to participate in social work schemes, as well as to promote self-employment projects among university graduates. In 1997 the bank was restructured, renamed and placed under the supervision of the Ministry of Social Planning with the view of reducing poverty. The objectives of the bank were extended to include providing the poor with production tools, inputs and with a focus on communal financing in rural areas.

The bank gives priority to group financing like Students' Unions, Women Associations, pensioners, and small amount of advances to individuals. It uses Musharaka, Murabaha and Ijarah ending with ownership, especially in financing means of transportation. The bank takes personal guarantee, group collateral and

local authorities guarantee. Table A4.1.1 in Annex reflects the SDB financing for the different sectors in the economy. It shows an increase in the total advances by SSDB bank as well as the direction of most finances to agriculture and industry. The share of handicrafts and small producers and social development schemes has also increased. The main problem facing SSDB bank was capital availability.

4.1.5 The Role of Non-Banking Funds in Relaxing Resource Constraints and Alleviating Poverty

The tendency towards liberalizing the economy in the last ten years had adversely effected the poor. The privatization program adopted and the efforts undertaken to reduce government expenditure led to the cut of several public programs, and consequently, many people lost their jobs. To counter-act these negative effects, many social funds have been established, and those existing have been activated. The Zakat Fund, the National Fund for Social Insurance, the National Fund for Pensions, the National Fund for Subsidizing Students and the Public Corporation for Medical Insurance were established to provide funds for helping the poor and financing social development programs. All funds in Sudan have to conform to Islamic fundamentals in their activities. This section will deal briefly with the role played by some of these funds in reducing poverty.

Zakat Fund

The official organization of Zakat in Sudan date back to 1980 when the Zakat Fund Law was issued and the Zakat collection and distribution have been entrusted to a government department. However, there were some interconnections between Zakat and taxes that resulted in some duality. In 1986, a new Zakat law was issued making Zakat obligatory and a separate Zakat Diwan has been established. The Zakat law has seen many improvements since then, and in 1990 and 2001 new amendments were introduced. The main objective of Zakat Diwan were stated as follows:

i. Collecting and distributing Zakat to achieving purity of wealth and providing social help and cooperation (Takaful).
ii. Advocating and enlightening people about the importance of Zakat.
iii. Emphasizing the role of the Islamic State in collection, distribution and management of Zakat funds.

The Zakat Diwan has 102 offices distributed all over the country. The main resources of Zakat are agriculture (50%), commercial activities (25%), animal resources, and gained money from transactions and self employment.

Table 4.1.6: Collections and distribution of Zakat 1995-2001 (Million Dinars)

	1995	1996	1997	1998	1999	2000	2001
Total collection	1714	3479	7179	8728.4	10700	11909.1	13461
Total distributions	1245.5	2413.3	8050.7	7528	8538.3	11490.6	12279

Zakat is distributed mainly to the poor and the needy, Islam advocacy (Dawa) and other specified channels. Beside this, the Zakat fund participates well in social development schemes such as medical and educational fields and water availability. Its participation in this area amounted to SD 2100 Million in FY2001.

Though these efforts of Zakat Diwan are very modest in comparison with the real needs of the poor, yet Sudan's experience in implementing obligatory Zakat is considered pioneer and the increase in the activities shown by table 4.1.6 emphasizes the perfection of efforts taken.

- **National Fund for Pensions**

The main objectives of this fund are:

1. Managing the pensions system according to the civil service law.
2. Collection of pensions premiums.
3. Development of resources through investment.
4. Improving the living conditions of pensioners.
5. Periodic increments in pensions.
6. Support of pensioners organizations and associations technically and financially.
7. Providing social services for pensioners and their families.
8. Adoption of poverty alleviation programs through supplying small production units for pensioners.

The number of beneficiaries as well as the resources of the fund had increased. The fund invests more than half of its resources in different development schemes and in financing some activities using Islamic modes of finance.

The Social development programs financed by the fund amounted to SD 930.4 million in FY2001. These were in the form of medical services, medical insurance, students' subsidies and other social development programs.

The National Fund for Social Insurance

The main objectives of this fund is to provide services for private and public sector employees. The fund has 34 offices distributed across the different states of Sudan. The fund resources accrue from premiums paid by the government and private enterprises and from sources like investment earnings ..etc.

The fund pays pensions according to the Social Insurance Fund Law. It also provides pensioners with medical insurance services, social subsidies, students' subsidies, orphans adoption and living cost subsidies.

Table 4.1.7: Resources and expenses of social insurance fund (1995-2001)
Million Dinars

	1995	1996	1997	1998	1999	2000	2001
Resources	371	1063	2209	3389	5264	7420	12738
Expenses	394	1302	2422	3452	3262	5921	8003

Source: National fund for social insurance.

The excess of expenses over resources during 1995-1998, was covered from previous reserves. The fund also invests some of its resources using the Islamic modes of Murabaha, Musharaka as well as other modes. Earnings from these investments were increasing and reached 37% of the fund total resources. On the expense side, social development comprises about 16% of total expenses. The fund investments increased much in the last two years to reach SD 2629 million in 2001.

This represents efforts to increase resources that can be directed to the fund beneficiaries and help reduce poverty.

4.1.6 Major Lessons

The role of Islamic banks in promoting development in Sudan is very clear from the increase of banks advances to agriculture, exports and social development. Yet, the results are considered far less than the ambitions to make full use of Sudan potentials and natural resources. This is attributed to the limited capital and resources available to banks. The comprehensive banking policy (1999-2002) was launched to form strong banking units and restructure them by increasing capital, merging, and privatization.

The used Islamic modes of finance reduced risks of the investors especially in the agricultural sector and thus encouraged producers to seek bank financing.

The guidelines booklets issued by higher Sharia Board, and the commitment by banks to abide by them is a distinguishing characteristics in establishing a good Islamic banking practice and corporate governance.

The role played by Sudanese banks in promoting social development and financing small farmers, handicrafts industries and productive families is a distinctive practice of applying Islamic principles of cooperation and helping the poor through Islamic financial institutions.

The experiences of some Sudanese banks practicing in these programs, though modest in quantity terms, proved that the Islamic Musharaka mode of finance could be very successful in removing small producers' fear from banks and the banks' reluctance to finance them. The shared risk makes it a win-win situation for both sides of the transaction.

The Sudanese experience of other social funds dealt with in the paper, showed that part of the poor's financing gab could well be filled by the social funds. Using Islamic modes to finance social development services and income generating small projects would help reduce poverty. Sudan experience in obligatory Zakat collection is successful in generating funds for social cooperation.

The pioneering experience of Sudan in establishing an Islamic stock exchange market, mutual investments funds and the securitization of equity ownership, all proved to be successful tools and mechanisms to provide liquidity and security to financing institution. Moreover, innovative Islamic financial instruments helped in mobilizing national savings and providing the monetary authority with Islamic monetary instruments for management and execution of monetary policy.

The sincere efforts of providing conducive and supportive jurisdiction and institutional framework helped establishing a good supervisory framework governing the Islamic investment funds and ensuring investors.

From the previous narration of Sudan's experience in Islamic financing of economic and social development many lessons can be drawn and are liable to be adopted:

1. The sincere efforts to establish effective Islamic financial institutions were complemented with the availability of conducive and supportive jurisdiction and institutional framework.
2. The Higher Sharia Board plays a major role in developing and innovating tools and instruments for the financial institutions as well as ensuring the conformity of these dealings and procedures to the Sharia.
3. The efforts made to develop practical aspects of Islamic modes of finance in Murabaha, Musharaka and Salam are distinguished and can be followed.
4. The obligatory Zakat in collecting funds for social cooperation.
5. The pioneer experience of Sudan in securitizing equity ownership of the central bank to provide Islamic instruments of monetary control and financing tools are good examples (Box 4.1).
6. The Khartoum Stock Exchange Market experience in organizing Islamic transactions in financial securities could be taken to resemble the base for development of Islamic money and capital markets.

4.2 Microcredit and Poverty Alleviation in Bangladesh

4.2.1 Introduction

A number of non-governmental (NGOs) and governmental organizations (GOs) have been working diligently for the last 25 years to eliminate poverty in

Bangladesh. Yet, there has been a very marginal gain in poverty alleviation exercise in Bangladesh. The fact that large numbers of population are affected by the fluctuations in incomes and earning induced by the seasonality of the agrarian economy ensures that there is a persistent demand for credit, which can allow flexibility of consumption and investment over time. The importance of credit is further emphasized when the difference between survival and uncertainty becomes visible during periods of generalized or specific disasters, whether those are floods, illness or diseases or market failure. The vulnerability makes the credit relationship a vital aspect of economic and social life in rural Bangladesh.

Over the last two decades the innovative microcredit programs run by the famous Grameen Bank and hundreds of NGOs have contributed to improving the quality of life of millions of people, mostly women, in Bangladesh. The success of Grameen Bank has encouraged hundreds of NGOs to start microcredit programs. Even today new initiatives are being taken to provide microcredit service. Microcredit has been proven to be an effective instrument for creating self-employment for millions of women and for increasing family income and consequently alleviating poverty (Hossain, 1988; Alamgir, 1998a). The mobilization of resources by these NGOs/MFIs is critical for expansion of outreach of such programs, i.e. bringing more women and men under such programs. The term microfinance institution (MFI) has been used in this report to indicate an organization which implements savings and microcredit program as the main program.

4.2.2 Bangladesh economic growth and poverty alleviation statistics

All development plans of Bangladesh have attached priority to poverty reduction as one of the major targets. A number of innovative poverty reducing programs has bean launched by the government and non-government organizations (NGOs) with remarkable access. As a result, the incidence of poverty has declined significantly by nearly twenty percentage points during the last three decades from 70 percent in the 1970s to about 50 percent in 2000. However, poverty has remained a pervasive feature of the country, as about 65 million people still live below the poverty line.

1. Trends in the Economy

Bangladesh achieved good growth performance during the 1990s. Between 1991 and 2000, real GDP in Bangladesh increased by 60 percent, averaging a growth rate of about 5 percent per year. Combined with the country's notable success in reducing the population growth rate over the past two decades, this economic performance resulted in real per capita GDP in the country rising by 36 percent over the decade, twice the 18 percent increase achieved by low and middle income countries during this period (WDR 2000/2001). Economic growth was most robust in the industrial sector. The industrial sector increased in importance from 21 percent to 26 percent of GDP, with real GDP in this sector increasing by an impressive 86 percent during the nineties. The export-oriented ready-made garment (RMG) sector recorded double-digit growth during this period.

The share of the services sector remained unchanged at about one-half of GDP, while agriculture – the slowest growing sector –declined in importance from 29 percent to 25 percent of GDP. However, even within the agricultural sector, there were notable achievements during this period, with the country attaining food grain self-sufficiency in FY2000 and aggregate production estimated at approximately 25 million tons. Despite the declining importance of agriculture in Bangladesh, this sector continues to be the main source of employment.

The impressive growth performance over the 1990s can, in large part, be attributed to prudent macroeconomic management, as well as to wide-ranging reforms introduced in the early 1990s. These reforms included steps to remove excess direct controls on economic activity, liberalize foreign trade, deregulate the investment climate, as well as in general introduce more market-oriented policies to create a more supportive policy environment for the private sector. Rapid integration with the global economy saw the ratio of the country's trade to GDP more than double over the decade. Domestic inflation remained at low levels throughout the decade.

2. *Trends in consumption-based poverty and inequality measures*

Consistent with the growth performance, survey-based consumption poverty estimates confirm that the 1990s were a period of declining poverty. Analysis of various Household Expenditure Surveys (HES) conducted by the Bangladesh Bureau of Statistics during the nineties shows that the incidence of poverty, as measured by both the upper and lower cost-of-basic needs (CBN) poverty lines, has fallen considerably (Tables 4.2.1 and 4.2.2). In FY2000, 50 percent of the country's population was poor (as measured by the upper poverty line), compared to 59 percent in 1991-92. Similarly, the extreme poverty rate (below the lower poverty line) declined from 43 percent in 1991-92 to 34 percent in 2000. Thus, according to both the upper as well as lower poverty estimates, the incidence of poverty in Bangladesh declined by about 9 percentage points over the course of the decade.

Although the progress on poverty is heartening, the overall incidence of poverty (50 percent) remains very high. Examining the total number of individuals living below the poverty line presents a sobering picture: the total population living below the upper poverty line in 2000 remained virtually unchanged (at about 63 million) compared to 1991-92, while the population living below the lower poverty line declined somewhat from 45.2 million in 1991-92 to 42.5 million in 2000.

Table 4.2.1 Trends in CBN Poverty Measures

	Upper Poverty Line			Lower Poverty Line		
	1991-92	1995-96	2000	1991-92	1995-96	2000
HEADCOUNT RATE (P_0)						
National	**58.8**	**51.0**	**49.8**	**42.7**	**34.4**	**33.7**
Urban	44.9	29.4	36.6	23.3	13.7	19.1
Rural	61.2	55.2	53.0	46.0	38.5	37.4
POVERTY GAP (P_1)						
National	**17.2**	**13.3**	**12.9**	**10.7**	**7.6**	**7.3**
Urban	12.0	7.2	9.5	4.9	2.6	3.8
Rural	18.1	14.5	13.8	11.7	8.6	8.2
SQUARED POVERTY GAP (P_2)						
National	**6.8**	**4.8**	**4.6**	**3.9**	**2.5**	**2.3**
Urban	4.4	2.5	3.4	1.5	0.7	1.2
Rural	7.2	5.3	4.9	4.3	2.8	2.6

Source: BBS and World Bank staff estimates.

Table 4.2.2 Regional Trends in Poverty

	Headcount Rate (%)			Annual Growth in mean Per-capita expenditures (%)
	1991-92	2000	Change	
All Divisions	**58.8**	**49.8**	**-9.0**	**2.4**
Chittagong	46.6	47.7	1.1	1.5
Dhaka	59.3	44.8	-14.5	3.2
Khulna*	59.6	47.0	-12.6	2.1
Rajshahi	71.9	61.0	-10.9	2.4

Source: BBS and World Bank staff estimates. * Including Barishal division

Progress on reducing poverty incidence was equal across urban and rural areas, but rural areas had better progress in reducing the depth and severity of poverty. Although average per capita expenditures increased much faster in urban areas, the overall decline in poverty incidence during the decade was roughly equal across the two sectors. However, trends in the P1 and P2 measures suggest that rural areas experienced greater reductions than urban areas in the depth and severity of poverty (Table 4.2.1).

A sectoral decomposition of the change in national poverty incidence into intra-sectoral changes and inter-sectoral changes due to migration suggests that the rural sector, with 80 percent of the population, contributed 78 percent of the total decrease in national poverty estimates between 1991-92 and 2000. The urban sector contributed about 10 percent of the national poverty decline. Migration from rural to urban areas where poverty is lower also decreased the national poverty rate, accounting for 10 percent of the decline.

Despite better progress in reducing extreme poverty in rural areas, most of the poor continue to reside in rural areas. By all consumption-based measures, poverty in rural areas continues to be higher than urban poverty. The rate of severe poverty remains twice as high as in urban areas (where the rate was 19 percent in

2000). Combined with the fact that over three-quarters of the population resides in rural areas, in Bangladesh overall, an overwhelming share (85 percent) of the poor continue to live in rural areas. Comparing across divisions, the largest number of the poor live in Rajshahi, followed by Dhaka and Chittagong divisions (Table 4.2.3). The HES data show real per capita expenditures to have increased by 27 and 16 percent respectively in urban and rural areas between 1991-92 and 2000.

Table 4.2.3: Total Number and Distribution of Poor in Bangladesh: 2000 HIES

	URBAN		RURAL		OVERALL	
All Divisions	**Number of Poor ('000)**	**% of Total**	**Number of Poor ('000)**	**% of Total 85%**	**Number of Poor ('000)**	**% of Total 100%**
	9,263	15%	53,478		62,741	
Chittagong	2,470	4%	13,455	21%	15,925	25%
Dhaka	3,652	6%	14,064	22%	17,716	28%
Khulna*	1,359	2%	9,756	10%	11,115	18%
Rajshahi	1,783	3%	16,203	26%	17,985	29%

Source: BBS and World Bank staff estimates. * Including Barishal division

4.2.3 Microcredit program in Bangladesh

1. Major NGO activities in Bangladesh

The occasional/partial failures of the market and the government gave particular impetus to the development of NGOs in Bangladesh. It is widely believed that the government has been failing to fulfill its own role due to slow bureaucratic process, administrative requirements without a human face and often 'politicization' of the administration. The market, on the other hand, is quite insensitive to the questions of poverty, nutritional requirements and disability, among others. With this background in place, where 'government' can hardly function properly and the market unwilling to address some of the key issues impacting on the lives the people of a developing country, the NGOs step in with the following innovations of 'new development paradigm'.

Firstly, NGOs in Bangladesh innovated the target group approach of rural development around mid-'70s against the backdrop of the obvious failures of trickle-down approach and cooperatives-approach to poverty alleviation. In fact, the new approach has strong operational framework of forming the rural poor with similar socioeconomic background into productive and associative units. These small members' unions provide new socioeconomic and quasi-political identity to the group members.

Secondly, NGOs introduced and popularized the micro-credit program for poverty alleviation around mid-'80s, along with three associated innovations: (i) the invention that the rural poor are credit-worthy and they can exploit self-employment opportunities if provided with small credit; (ii) rural credit markets can have a new financial instrument, small credit associated with collateral in the form of group

pressure and peer monitoring; and (iii) the rural poor women can be a reliable clientele group. While Grameen Bank deserves special mention as innovator of micro-credit, others have contributed to its refinement. NGOs in Bangladesh rightly identified the extent and severity of poverty along with the associated multidimensionality of it as well as the working methods with rural poor people through the micro-credit program. The original 'success story' – the Grameen Bank - is currently imparting necessary technical assistance in terms of field training through 'dialogue programs', monitoring and evaluation services etc. to the replicators worldwide.

Thirdly, NGOs are credited to fruitfully utilize 'the participatory approach' in every stage of the program. Unlike the 'conventional wisdom' of 'top-down' planning models, the NGOs devised a 'participatory development' model whereby they try to use the 'indigenous' local knowledge. As this process calls for an active beneficiary participation, the beneficiaries in fact 'own the program'. As the NGOs' project experience shows, the outcome of such projects is seldom negative.

Fourthly, as indicated earlier, NGOs innovated the concept of 'empowerment' to bring the poor and other disenfranchised groups into the forefront of development agenda in Bangladesh. At a basic level the notion of empowerment entails a shift in relationships through which the balance of power tilts more in favor of the poor. The objective is to strengthen the 'voice' of the poor in society – an objective that has entered the development lexicon of both NGOs and donors in Bangladesh. A large number of beneficiaries in micro-credit and other social programs launched by NGOs are rural poor women. Most NGOs in Bangladesh have an explicit concern and commitment to women and empowerment.

Finally, NGOs have contributed in innovating institutions for the poor. The process of institution building has been through development of human resources with the help of education and conscientization. With a greater awareness of the socioeconomic and political dynamics affecting their life, and with a collective force generated through their sense of belonging to their own institutions, the poor are able not only to mobilize and manage their own resources, but are also motivated to have their voices heard in shaping policies and plans that affect their lives. Most development NGOs have operationalized this paradigm by initiating people's organizations at the grass-root levels and facilitating the release of a latent but potent social energy to mobilize resources and to have political expression for distributive justice.

2. *Overview of Microcredit Program in Bangladesh:*

The poor and the landless in Bangladesh, and elsewhere as well, do not have access to formal financial system for credit (UNDP, 1995). However, recently some commercial banks have introduced microcredit for the poor following the path of the Grameen Bank and NGOs. Although these initiatives are admirable they are limited in coverage. Expectedly the commercial banks - their human resources, structures, and products are not geared to serve the poor. Their targets are very

different sectors of the economy. The formal financial system is based on collateral, which the poor do not have and it requires huge paper work to process a loan. Eventually, the poor resort to informal sector, e.g. moneylenders, for credit to meet their consumption and investment needs and pay usurious rates of interest. But there exists huge demand for small amounts of credit by the poor for investment. To circumvent the situation, Professor M. Yunus of the world famous Grameen Bank, has innovated a system of credit delivery to the poor without collateral, popularly known as microcredit (see Box 4.2). Presently, microcredit has reached an unprecedented scale and is expanding fast in Bangladesh. All major NGOs are expanding their outreach by including new members as well as raising the average credit per member. The poor men and women are mobilized into groups to receive credit so that they take the responsibility of repayment of each other's loan.

Generally, MFIs serve the lower income groups who often have very limited assets. Traditional collateral for obtaining bank loans like property, land and machinery are mostly not available to them. So, usually, the mechanism of MFIs does not charge collateral security for providing loans. Rather they have introduced some innovative methods to minimize the risks of their operations. They use some collateral substitutes and a number of alternative forms of collateral for reducing the risk of loan loss. One of the most commonly used collateral substitutes is peer pressure, either on its own or jointly with group guarantees. Group guarantee of the group members is a very popular form of collateral on the part of many MFIs. MFIs facilitate the formation of group and group members provide guarantee for each other's loan. The guarantees may be also of two kinds. In one case, no member is able to have access to a loan if all members are not current in their loan payments and in the another case, all members are equally liable if other group members default on their loans. Some MFIs even require group members to contribute to a group guarantee fund, which is used if one or more borrowers fail to repay. Some MFIs lend to people of a particular community based on their good reputation. In some cases, when a new borrower is unable to provide security, credit officers rely heavily on information as a collateral substitute. Maintaining close contact is the most effective collateral substitute for the small credit to the poor.

There are some popular alternative forms of collateral used by the micro financial institutions. One of the most widely used forms is the provision of compulsory savings. It implies that the clients must save a certain percentage of money to obtain credit from the institutions. This is usually kept in the form of percentage of loan or some times known as contributions to group funds. This cannot be withdrawn when the loan amount is outstanding. This is a form of saving which is made compulsory for most of the MFIs' clients and is different from voluntary savings that generally permits withdrawal of fund. Most compulsory savings are available for withdrawal only at the end of the loan term. This also works as the contributory factor for the development of the saving habits in the poor. Sometimes assets are pledged (such as furniture, appliances, etc.) as security to realize the loan amount. This sends the message to the borrowers that the MFI is serious about loan repayment. Personal guarantees from friends, relatives or any respected persons of the area are also accepted as security by some MFIs.

Box 4.2 The Typical Microcredit Program

The typical microcredit program has the following loans key features: (a) It is collatera-free so that the poor and the landless may easily avail of it. (b) To get loans, the poor members are mobilized into groups, ranging from 5 to 30 members by a particular MFI. (c) The members meet once every week and make small savings deposit with the concerned MFI. After certain waiting period, which usually varies from 2 weeks to 6 months, members receive loans, taking collective responsibility for repaying the same. (d) Loans are usually given for one year and recovered in weekly installments. A few MFIs recover loans in monthly installments. (e) The field staff of MFIs supervises utilization of loan. (f) The loans are usually provided for common petty trades, and other activities in rural areas, so that the members can pay weekly installments. Some organizations give more than one loan to their members, like house loan, seasonal agricultural loan etc. (g) the majority of the borrowers (as high as 90%) are women. (h) MFIs usually set branches in remote areas to help the poor members in receiving loan. The field staff collects loan installments at the meeting held at the members' premises. The procedure for receiving loan has been greatly simplified making the program very attractive to the poor and the illiterate villagers. The MFIs have simple but detailed accounting and management information system to handle large number of borrowers. (i) The MFIs start with small loan (Taka 1-3 thousand, or US$ 25 to 75) and provide repeated loans of increasing amount as long as repayment of earlier loan is satisfactory. This system allows continued flow of credit fund since poor need regular access to credit to maintain and to expand their economic activities.

Source: Outsourced study on Micro-finance in Bangladesh 2002.

4.2.4 A Comparison of 12 secular and Islamic micro-credit NGOs in Bangladesh

1. Sample of Islamic and secular NGOs

There are only handful of NGOs currently operating in Bangladesh that provide microfinancial services based on Islamic financing. This is a very recent phenomenon. Consequently, these NGOs are very small in terms of their membership. The Rural Development Scheme of Islamic Bank Bangladesh Ltd. is the largest in this sector. We have selected 5 NGOs and RDS to make the comparison. These are small NGOs and relatively inexperienced. For the sake of comparison, NGOs of similar size have been selected. However, these NGOs are relatively more experienced and have been operating in this sector for several years. For comparison of these two groups of NGOs the emphasis has been on the system and the mode of operation of microfinance programs.

2. Critical Findings of the Islamic and Secular NGOs

Survey results are given in Table A4.1.1 in Annex, from which we can make the following observations regarding the similarities and differences of secular and Islamic NGOs.

Islamic NGOs are late in coming to the field of rural development in general and microcredit/micro-investment in particular. On the other hand several hundred secular NGOs have been implementing microcredit programs since 1980s. Discussions with leaders of Islamic NGOs reveal that they were late to

appreciate the roles of NGOs and in fact had hostile opinions about activities of secular NGOs. Gradually, some of them appreciated that credit programs can be implemented by blending Islamic principles of investment and the mechanism of mobilizing the poor that is the management practice of implementing microcredit programs.

Islamic NGOs have been managing mainly micro-investment/microcredit programs while secular NGOs are implementing other programs like non-formal education, health and sanitation, mainly with the financial assistance of external donors.

In microcredit program both groups of NGOs follow the same selection criteria to select their program beneficiaries. In fact Islamic NGOs are following the existing norms of selecting the poor people in rural areas. Normally the land ownership criteria such as families having maximum of 0.5 acres of land included in the programs.

Gender issues: Existing bias among NGOs is to include mostly women in their programs. Islamic NGOs are including both men and women. However, there are extreme examples where one Islamic NGO (Islamic Cultural Society), which accept men as members, and Islamic Bank accepts mainly women like secular NGOs.

Microcredit mechanism: Islamic NGOs have basically copied the microcredit mechanism developed by the Grameen Bank and followed by all NGOs in Bangladesh. However, there might be small variations introduced by each NGO to suit its own situation. The basic mechanism is as follows: poor women and men are organized in groups who take responsibility of repayment of each other's loan at the event of default. Groups meet once a week to make the transactions, deposit savings and pay loan installments.

One basic requirement for receiving loan is to deposit small amount of money as 'compulsory savings'. Islamic NGOs also follow the same procedure because it gives the poor members an opportunity to mobilize own capital. It is a kind of cash collateral for the NGO and part of the loan/investment operations may be financed by this fund. However, one important distinction may be noted here regarding payment of interest on members' deposit. Secular NGOs pay a fixed rate of interest, 5-6% per annum, on deposit. On the other hand, Islamic NGOs provide variable rate similar to the Islamic Banks. The rate is computed at the end of the year considering the total income, deposit and expenses.

Normally NGOs do not allow members to withdraw their savings deposits. In case of Muslim Aid it allows members to withdraw their savings. The most significant difference between the Islamic NGOs and other NGOs centers on the issue of interest. Secular NGOs charge at the rate of 20-30% per annum on the cash credit provided to the members. However, Islamic NGOs do not provide any cash loans. They apply the concept of 'Bye Muajl' (sale on credit) and provide commodity adding certain percent of mark-up on the cost of the commodity. The

rates vary among the organizations. For example, Islamic Bank adds 12% and Muslim Aid Bangladesh adds 12.5% on the cost over a period of one year. Since the payments by the members are made every week, when computed according to the method of finance the corresponding rate of interest will be approximately 24% and 25% respectively.

The other terms and conditions of credit of these two groups of NGOs are similar. The loans are given for a period of one year and recovered in weekly installments. The amount of loan for both groups of NGOs varies between Taka 3000 to Taka 10,000.

The activities financed by both group of NGOs are the same; the commonly available petty activities in the rural areas. Examples are poultry and livestock rearing, petty trade, financing agricultural inputs, rural vehicles, housing material, handlooms etc.

Sources of fund: Common sources of fund for microcredit programs are members' savings, grants from external (western) donors and currently from the Palli Karma Sahayak Foundation (PKSF), an organization established by the Government of Bangladesh to provide loan to successful NGOs. Islamic NGOs are fund-starved although they have ample opportunities to expand and there is strong demand in the rural areas for Islamic microfinancial services. Only Islamic Bank has adequate resources to expand its microfinancial services. Four Islamic NGOs in the sample received some fund from PKSF. International Islamic donor agencies normally do not provide fund for microcredit, they are more interested in relief and rehabilitation programs. Islamic NGOs also lack guidance for improving their management and professional skills. That makes Islamic NGOs as followers rather than leaders in this sector.

Future Trends: Both groups of NGOs will be focusing on two issues: expansion of programs by accepting more and more members and achieving financial viability of the programs.

4.2.5 Micro-credit impact in Bangladesh: Analysis of data

The total number of registered NGOs operating in Bangladesh is given in Table 4.2.4. In the 1970s, there were 40 NGOs, 19 of them foreign, working in the country. Their numbers surged in the 1990s to such an extent that around 1500 NGOs were registered with the NGO Affairs Bureau (NGOAB). However, not all NGOs are registered with the NGOAB. Thus the actual number of NGOs could be much more than what official statistics say.

Table 4.2.4: Growth of Development NGOs in Bangladesh in the 1990s

Period	Number of NGOs Registered			Number of Active NGOs		
	Local	Foreign	Total	Local	Foreign	Total
1990-91	102	10	112	395	99	494
1991-92	129	12	141	523	111	634
1992-93	77	14	91	600	125	725
1993-94	106	9	115	683	124	807
1994-95	108	5	113	790	129	919
1995-96	92	3	95	882	132	1014
1996-97	115	3	118	997	135	1132
1997-98	99	8	107	1096	143	1239
1998-99	119	3	122	1215	146	1361
1999-2000 [a]	123	10	133	1338	156	1494

Note: a. Data up to May 2000; Source: NGO Affairs Bureau, Prime Minister's Office, July 2000.

Based on the data collected over the period December 2000 to June 2001, we report performance of a total number of 601 MF-NGOs. The number of reported MF-NGOs has increased from 585 to 601, registering 2.74% increase during last six months (December 2000 to June 2001). Total active members of the reported 601 NGOs were 11,604,803, which has increased by 5.29% during last six months. The male members constituted 15.30%, which has decreased by 0.49% during the same period. Comparison of 487 common NGOs shows that the active members were increased by 4.02% during the period. Table 4.2.5 shows that outstanding borrowers of the 601 MF-NGOs were 8,319,158 as of June 2001, which is 4.13% higher than that of previously reported 585 MF-NGOs during the last six months. Comparison of 487 common MF-NGOs shows that the number of outstanding borrowers has increased by 5.06% during the period.

Table 4.2.5: Performance Comparison of Microfinance Program (December 2000 to June 2001)

	Particulars	Data of 585 MF-NGOs (as of December 2000)	Data of 601 MF-NGOs (as of June 2000)	% change*
1	Total active member (nos.)	11,021,663	11,604,803	7.0
2	Total active male member	1,739,994	1,775,003	3.4
3	Total active female member	9,281,669	9,829,800	7.7
4	Total outstanding borrower	7,988,831	8,319,158	5.1
5	Total disbursement (in million Taka)	125,607.61	143,983.25	15
6	Total outstanding loan (in million Taka)	21,903.47	23,983.23	10.6
7	Net savings (in million Taka)	8,886.02	9.590.72	9.7

Source: *CDF Statistics, Vol-11 & 12, CDF, Dhaka.* Conversion rate: 1 US$ = 57.23 Bangladeshi Taka (BDT)

- Percentages have been calculated considering the common set of 487 organizations in both the periods.
- MF-NGO: Microfinance Non-governmental Organization

Table 4.2.5 shows that cumulative disbursement of NGOs was Taka 143,983.25 million (91.53% in rural areas and the rest in urban) as June of 2001, which is 14.63% higher than that of previously reported 585 MF-NGOs during the last six months. Comparison of 487 common MF-NGOs shows that the amount of cumulative disbursement was increased by 14.99% during the period. Table 4.2.5 shows that total loan outstanding of reported MF-NGOs was Taka 23,983.23 million as of June 2001, which is 9.50% higher than that of previously reported 585 MF-NGOs during the last six months. Comparison of 487 common MF-NGOs shows that the amount of outstanding loan was increased by 10.63% during the period. Table 4.2.5 shows that total net savings of the reported 601 MF-NGOs was Taka 9,590.72 million as of June 2001, which is 8.17% higher than that of previously reported 585 MF-NGOs during the last six months. Comparison of 487 common MF-NGOs shows that the amount of net savings was increased by 9.68% during the period.

As of June 2001, 601 MF-NGOs received Taka 32,328.32 million from external and internal sources for the revolving loan fund. The major external sources include foreign donation 17.43%, members' savings (25.74%) and PKSF (23.50%). A major portion of the funding (17.21%) was also generated from service charges. The contribution of local banks, international NGO and donor to RLF is seemingly decreasing, while the contribution of members' savings, PKSF and service charge is increasing. The details are given in Table 4.2.6. During the period of 1983-84 to 1995-96 the members' savings have exhibited an overall growth of 43%, while it has increased by 20% over the last year. PKSF's contribution has been also continuously increasing and registered 66% growth. During the period foreign donation has also increased at a slower rate of 9%. The service charge made an enormous contribution of 36% growth in the RLF (revolving loan fund). Average recovery rate has been worked out to be 95.40%. The rate of service charge on loan has been found varying from 2.50% to 20% in the flat method and 11% to 36% in the declining balance method. Out of 601 MF-NGOs 98.50% practice the flat method.

Table 4.2.6: Sources of Revolving Loan Fund (RLF) of microfinance Program (December 2000-June 2001)

Sources	No. of MF-NGOs received fund*				Amount (in million Taka)		As percentage of total RFL	
	Dec. 2000	%	June 2001	%	Dec. 2000	June 2001	Dec. 2000	June 2001
Member's savings	545	93	563	94	7,607.23	8,321.90	25.47	25.74
PKSF	118	20	119	20	6,862.82	7,598.66	22.97	23.50
Local Bank	52	9	48	8	2,9 28.51	2,959.57	9.80	9.15
International NGO	73	12	64	11	160.71	166.99	0.54	0.57
International Donor	162	28	154	26	5,383.64	5,466.04	18.02	16.91
Service charge	417	71	398	66	4,768.08	5,563.28	15.96	17.21
BRAC	55	9	58	10	69.01	71.80	0.23	0.22
ASA	17	3	17	3	26.51	22.37	0.09	0.07
Proshika	182	31	200	33	55.02	63.30	0.19	0.20
Own fund	379	65	391	65	1,066.87	1,338.96	3.57	4.14
Others	224	38	250	42	944.77	755.45	3.16	2.34
Total		**585**		**601**	**29,873.16**	**32,328.32**	**100.00**	**100.00**

Source: *CDF Statistics, Vol 5– 11 & 12, CDF, Dhaka. *Multiple response*

Table 4.2.7 shows that credit disbursement to small business sectors is getting priority. On the other hand agriculture, food processing, transport, housing and livestock were getting less priority during the same period. Disbursement to fisheries sector got priority the same period, where cottage industries, health and education sectors got almost equal priority in the same period. Table 4.2.8 reveals that 16.72% NGOs have outstanding loan in the range of Taka 0.2-0.5 million followed by 15.89% in the range of Taka 0.5-1.0 million, 15.38% in Taka 1-2 million and 10.37% in Taka 2-4 million. So more than half of the NGOs have outstanding loan between more than Taka 0.2 million and Taka 4 million. Again 44.82% NGOs are operating with outstanding loan up to Taka 1 million. Only 2.67% NGOs have portfolio above Taka 100 million.

Table 4.2.7: Sub-sector-wise Microfinance Disbursement

Sub-sector	% disbursed up to June 2000 (476 MF-NGOs)	% disbursed up to December 2000 (469 MF-NGOs)	% disbursed up to June 2000 (469 MF-NGOs)
Agriculture	12.63	12.77	12.23
Fisheries	4.74	4.81	4.91
Food Processing	6.99	7.11	3.78
Small business	41.31	41.81	43.02
Cottage industries	3.03	3.08	3.03
Transport	3.42	3.49	2.78
Housing	1.28	1.30	1.16
Health	0.39	0.37	0.45
Education	0.02	0.02	0.08
Livestock	20.91	20.53	18.11
Others	5.28	4.71	10.45
Total	**100.00**	**100.00**	**100.00**

Source: CDF Statistics, Vol – 10, 11, and 12 CDF, Dhaka

Table 4.2.8: Distribution of Outstanding Loan Amount

	Group (in Taka)	Total MF-NGOs	% of total
1	<=50 thousand	18	3.01
2	> 50-100 thousand	21	3.51
3	> 100-200 thousand	34	5.69
4	> 0.2-0.5 thousand	100	16.72
5	> 0.5-1 million	95	15.89
6	> 1-2 million	92	15.38
7	> 2-4 million	62	10.37
8	> 4-8 million	57	9.53
9	> 8-16 million	43	7.19
10	> 16-32 million	37	6.19
11	> 32-64 million	18	3.01
12	> 64-100 million	5	0.84
13	> 100-200 million	6	1.00
14	> 200-500 million	4	0.67
15	> 500 million	6	1.00
Total		**598**	**100.00**

Source: *CDF Statistics, Vol 5– 11 & 12, CDF, Dhaka. *Multiple response*

Table 4.2.9 shows that around 32% NGOs have mobilized savings in the range of Taka 100,000-500,000, which is the highest number in the distribution group. Fifty nine percent of MF-NGOs has savings up to Taka 1 million and 10.17% NGOs have above Taka 10 million. Table 4.2.10 shows that about 53.82% of the reported NGOs give 6-7% interest on savings to the members while an insignificant number of NGOs practice more than 10%. It appears that the interest rate on saving offered by NGOs is not much encouraging for mobilizing more saving as different savings products of government and commercial banks offer higher rate of interest. Table 4.2.11 shows that the pattern of service charge (flat method) practiced by most of the NGOs. About 85% NGOs charge 11-15% on loan and 11.65% NGOs practice 16-20%. About 4% NGOs charge below 11% and no NGOs practice above 20%, which is the remarkable in microfinance sector of Bangladesh.

Table 4.2.9: Distribution of Net Savings Mobilization

	Group (in Taka)	Total MF-NGOs	% of total
1	<=50 thousand	34	5.67
2	>50-100 thousand	32	5.33
3	>100-500 thousand	192	32.00
4	>500,000-1 million	96	16.00
5	>1-2 million	72	12.00
6	>2-4 million	55	9.17
7	>4-8 million	40	6.67
8	>8-10 million	18	3.00
9	>10-50 million	46	7.67
10	>50 million	15	2.50
Total		**600**	**100.00**

Source: *CDF Statistics, Vol 5– 11 & 12, CDF, Dhaka. *Multiple response*

Table 4.2.10: Rate of Interest on Savings

SL	Group of interest rate (%)	Number of MF-NGOs	% of MF-NGOs
1	Up to 5	133	25.38
2	6-7	282	53.82
3	8-10	95	18.13
4	11-15	13	2.48
5	16-20	1	0.19
Total		**524**	**100.00**

Source: *CDF Statistics, Vol 5– 11 & 12, CDF, Dhaka. *Multiple response*

Table 4.2.11: Service Charges (Flat Method) on Credit

SL	Group of interest rate (%)	Number of MF-NGOs	% of MF-NGOs
1	Up to 10	21	3.55
2	11-15	502	84.88
3	16-20	69	11.65
Total		**592**	**100.00**

Source: *CDF Statistics, Vol 5– 11 & 12, CDF, Dhaka. *Multiple response*

Table 4.2.12 shows that out of a total 601 NGOs, 357 NGOs have active members up to 2,000, 101 NGOs have members from 2,001 – 4,000. Thus around 76% NGOs have members up to 4,000. On the other hand, 135 NGOs (22.48%) have members ranging from 4,001 – 80,000. Only 5 NGOs have members more

than 320,000 (i.e., BRAC: 3.74 million, Proshika: 2.30 million, ASA: 1.33 million, Swanirver Bangladesh: 0.72 million, and Caritas Bangladesh: 0.33 million). These statistics imply that medium and few big-sized NGOs are predominant in the sector.

Table 4.2.12: Distribution of 601 MF-NGOs by Outreach (Active Member)

SL	Group of active members (numbers)	Number of MF-NGOs	% of MF-NGOs
1	<=500	117	19.47
2	501-1000	122	20.30
3	1001-1500	74	12.31
4	1501-2000	44	7.32
5	2001-3000	71	11.81
6	3001-4000	30	4.99
7	4001-5000	18	3.00
8	5001-6000	16	2.66
9	6001-7000	12	2.00
10	7001-8000	11	1.83
11	8001-9000	12	2.00
12	9001-10000	9	1.50
13	10001-20000	28	4.66
14	20001-40000	18	3.00
15	40001-80000	11	1.83
16	80001-160000	1	0.17
17	160001-320000	2	0.33
18	>320001	5	0.83
Total		**601**	**100**

Source: *CDF Statistics, Vol 5– 11 & 12, CDF, Dhaka. *Multiple response*

From the common set of 487 microfinance NGOs it has been found that total active members have increased by 7.02% during December 2000 to June 2001 while it is 5.06% in the case of outstanding borrowers."

4.2.6 Summary and policy suggestions

The recent development of microfinance has made it possible to expand financial services to reach a larger segment of the poverty-stricken population. Public interest in promoting the growth of microfinance is due to the realized difficulty in providing financial services to this target population and its potentially welfare-enhancing characteristics. The challenges of microfinance are derived from a number of factors which include: the transaction services being expensive, the risk involved in lending to poor clients and the costs involved in lowering these risks is high, and risk of losses from default is high. MFIs must usually overcome several severe difficulties in order to successfully provide financial services to the poor. Therefore, the role of public policy should be to create conditions for the development of sustainable and profitable MFIs. Successful MFIs are willing and able "to charge interest rates that cover their costs, have designed products that match the demand from the clients in the market niches where they operate, and have adopted lending procedures that lower borrower transaction costs" (Gonzalez-Vega, 1998).

Sustainability is the ability of the MFI to reach goals in the short term without harming its ability to meet long-term goals. Therefore, to prevent their future demise it is crucial that MFIs establish procedures that will assist them in becoming both operational and financially self-sufficient. Also, the image of the sustainability of an MFI promotes loan repayment in the cases were there is no physical collateral because borrowers value the sustainability of an MFI, creates depositor confidence, attracts commercial funds to the MFI, and reduces employee turnover while increasing employee commitment to the organization.

By eliminating the need for collateral and implementing a banking system rooted in mutual trust, the Grameen Bank reversed conventional banking procedures. The banking system created by the Grameen Bank relies heavily on the participation of its members and instills in them accountability. Now the largest rural finance institution in Bangladesh, the Grameen Bank has been an inspiration to thousands. Individuals from over a hundred countries have experienced Grameen's training and have attempted to bring its philosophy back to their countries. Currently, approximately 223 replicated systems in 58 different countries have been established. However, although these systems exhibit different features, the underlying premise of each is to provide a credit delivery system suitable to provide loans to the poor.

Grameen Bank's accomplishments to date are very promising. Through the availability of microcredit, the poor in Bangladesh are being given hope and the possibility of improving their lives through the use of their own labor. The bank has provided the poor with the opportunity to purchase the necessary equipment and other means of production in order to start their own income-generating ventures through self-employment or another form of people-based production. In addition to this, Grameen Bank is slowly making in-roads to correct some of the social ills associated with the Bangladesh culture. Many believe the viscous cycle poverty cannot be overcome unless many of the social disadvantages faced by the poor can be properly addressed. Through its housing program and medicare scheme, the Grameen Bank has concentrated much of its efforts eliminating some of the social conditions faced by the poor in Bangladesh through education and financial benefits.

Admittedly, all of the evidence supporting the Grameen Bank is not positive. Some studies claim that instead of lifting people from poverty, microfinance instead saddles the poor to a lifetime of perpetual debt, actually making their situation worse. Also, there is some debate whether microfinance institutions can ever be profitable and Grameen Bank is no exception. Grameen Bank, while it appears sound financially, relies heavily on subsidies and charitable contributions to sustain its operations. Despite the negative evidence, there is much to be encouraged about. Grameen Bank has improved the lives of many. Women in particular are improving their status in the Bangladesh society. The Grameen Bank realized early on that by providing credit to women not only improved the economic condition of the family but also greatly enhanced the social dimensions as well.

4.3 The Role of the HIPC Debt Relief Initiative and SMEs in Bridging the Resource Gap for the Financing of Poverty Reduction Programmes: the Case of Uganda.

4.3.1 Introduction

Prior to the HIPC debt initiative, Uganda's debt service ratios were unsustainably high. For example debt service as a percentage of exports of goods and non-factor services was 71.2% in 1992/93. Apart from the strong export performance associated with the coffee boom in the mid-1990's, the decline in the ratio over the period to 19.8% in 1996/97 was a result of increased debt rescheduling efforts and accumulation of arrears, which was simply a postponement of the actual debt problem. In a situation where government is overburdened with debt service resulting from meager export earnings and the small tax base, the social sectors tend to face severe cuts in expenditure, as was the case in Uganda before the HIPC debt initiative.

Although it is still in early stages, the HIPC debt initiative has helped bridge the resource-gap in Uganda and has thus helped increase government expenditure on poverty-reducing programmes. The HIPC has, therefore released resources, that would have otherwise been used for debt service, for investment in poverty reducing social sector programmes. To date, these resources which are channeled through the Poverty Action Fund (PAF), are an integral part of the Medium-Term Expenditure Framework (MTEF).

A part from the role played by the HIPC debt relief in mitigating resource constraints through increased budgetary provisions to social sector programmes that are poverty-reducing, Small and Medium-Scale Enterprises (SMEs) have also played an integral part in the drive towards poverty eradication. By increasing the asset accumulation process, employment and enhancing the income earning capacity of the poor, SMEs have made a positive contribution to poverty reduction.

This section presents an assessment of the extent to which the HIPC debt initiative has bridged the existing resource gaps in the Ugandan economy. It specifically assesses the performance of the key sectors identified in the Poverty Eradication Action Plan (PEAP)/Poverty Reduction Strategy Paper (PRSP), which are financed from the HIPC savings. In addition, this section also discusses Uganda's experience with SMEs and their role in poverty reduction.

4.3.2 Evolution of Uganda's Debt Problem and Resource Constraints

1. Evolution of Debt

Following the economic and structural breakdown of the Ugandan economy in the 1970s, an attempt at coordinated policy reforms was made in 1981, when the government received financial and technical support from the International Monetary Fund (IMF) and the World Bank. This marked the start of the Stabilization and Structural Adjustment Programmes (SAPs) and involved the implementation of

policy reforms aimed at reviving the productive capacity of the economy. The policy package included restoring price stability and producer incentives; rehabilitating physical infrastructure; improving capacity utilization in the manufacturing sector; and instilling discipline, accountability and efficiency in the public sector. It was during this time that Uganda's external debt position started deteriorating. This programme however collapsed in 1984 after the IMF/World Bank cut-off lending to Uganda, following the latter's failure to meet the programme benchmarks. However, with the incoming of a new government in 1986, the second and more successful phase of economic reforms was launched in May 1987. The broad policy objectives of this reform effort focused on:

(i) the need to stabilize the economy, through the restoration of fiscal and monetary discipline, notwithstanding the increasing demands for considerable outlays to rehabilitate the devastated infrastructure in this post conflict economy; (ii) the liberalization of consumer and producer prices; (iii) the progressive movement towards a realistic, market determined exchange rate within a system free of exchange restrictions and distortions; (iv) the strengthening of the Balance of Payments (BOP) and the normalization of relations with external creditors; (v) the removal of trade restrictions; (vi) the privatization and rationalization of state enterprises; (vii) the liberalization of interest rates within a restructured and more efficient financial system capable of mobilizing savings and increasing investments, with a view to raising the rate of economic growth.

2. Resource Constraints

The low domestic savings rate, narrow revenue base including inadequate export earnings, the acute need of resources to rehabilitate the economy in order to revive the productive capacity and improve government ability to manage the economy necessitated substantial reliance on external assistance. As shown in table 4.3.1 below, the Gross Domestic Savings (GDS) on average during the period 1989 to 1999 fell short of Gross Domestic Investment (GDI) by about 10 percentage points of GDP. However, the Gross National Savings (GNS), which include private transfers and grant financing of the government budget, reduced this resource gap to an average of 7 percentage points over the same period. What is worth noting is that the average GNS in the latter years of 1994-1999 reduced this gap to about 4 percentage points of GDP largely as a result of increased grant financing of the budget deficit. This gap in the latter years was closed with highly concessional loan financing.

While the annual GDP growth averaged 6.5 per cent over the period 1989-1999, the investment rates did not increase significantly to warrant such a growth rate. This growth can be explained by two factors: first the increased capacity utilization which followed the implementation of prudent macroeconomic policies in addition to rehabilitation of physical infrastructure and second, the coffee boom of the mid-1990's. It can therefore be appreciated that these high growth rates while, necessary for poverty reduction can not be sustained without increased investment ratios. On the other hand, poverty reduction is necessary for sustained GDP growth rates particularly in the Uganda economy where the consolidation of post-conflict

peace depends a lot on the creation of economic opportunities and poverty reduction. It is therefore against this background that the Ugandan government has identified the need to reduce poverty through broad-based growth that involves the participation of the poor. The need for investment in poverty-reducing sector is therefore high on the government agenda. However, given the resource gaps identified on account of low GDS, the role of external financing becomes crucial in closing these gaps. The HIPC Debt Initiatives is thus one of the channels through which government is meeting this challenge.

Table 4.3.1: Uganda: National Accounts (as a percentage of GDP)

	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999
Gross National Savings	1.9	0.6	1.4	2.1	3.0	10.4	12.1	10.8	12.8	13.4	10.5
Gross Domestic Savings	1.0	0.6	0.7	0.4	1.1	4.3	7.4	4.6	8.0	5.6	4.9
Gross Domestic Investment	11.1	12.7	15.2	15.9	15.2	14.7	16.4	16.1	16.1	15.0	16.4
Gross Public Investment	5.4	6.2	7.4	7.4	6.7	5.4	5.4	5.3	4.7	4.6	4.7
Gross Private Investment	5.7	6.5	7.8	8.5	8.5	9.2	10.2	11.3	11.6	10.5	11.7
GDP Growth Rates	6.4	6.5	5.6	3.4	8.3	6.4	11.5	8.6	5.1	4.6	7.9

Source: African Development Indicators 2001 and selected Statistics on African Countries, ADB.

Although the Ugandan investment ratios relative to the sub-Saharan African (SSA) ratios have been low during the period 1989-1999, these are expected to increase in the medium term largely on account of private sector investment given the investor confidence that has been created in the economy. To date, the trend is such that public investment rates have been declining while private investment rates are on the rise. Initially, the government had to invest heavily on physical infrastructure rehabilitation so as to attract private sector investment. It has now shifted its investment mainly to poverty reducing sector programmes.

Given the savings-investment gaps identified above, the reliance of the adjustment effort on external loan financing during the 1990s created a relatively large debt burden for Uganda. As a result, Uganda's external debt more than doubled during the adjustment period reaching US$ 3.54 billion as of June 1997 up from US$ 1.6 billion in 1987. A large part of the increase is attributable to credits obtained from multilateral institutions on highly concessional terms to support the BOP and finance development projects. The Multilateral debt as of June 1996 accounted for about 75 percent of the total debt stock, compared with only 43 percent in 1987, making the debt unsustainable as shown by the indictors in Table A4.3.1 in the Annex.

Uganda's total external debt as a percentage of exports of goods and non-factor services remains high although it declined from over 1500% in 1992/93 to 535.5% in 1996/97 before rising to 792.1% in 1997/98. The reversal in the trend observed in 1997/98 is largely attributed to the unwinding of the coffee boom. Basically, the ratios of debt service–to–export and total external debt to GDP

remained relatively high during the same period while arrears continued to accumulate (Table A4.3.1).

Given the inadequate resource envelope and the mounting debt servicing burden, the government expenditure cuts on public infrastructure and basic social services, such as education and health, which are critical for enhancing human development, became inevitable. Indeed as indicated in table A4.3.2, external loan repayment accounted for over 27% of Uganda's recurrent expenditure in 1992/93 and 1993/94, which was higher than the allocation to education, health, community and social services, and public order and safety. In 1994/95, the share allocated to external loan repayment including interest declined largely on account of accumulation of arrears and debt rescheduling. It however rose in 1998/99 on account of payments to some multilateral financial institution before declining in 1999/2000 because of the HIPC debt initiative. The share of the health sector in total recurrent expenditure was generally stagnant, where as the share of education rose only after the introduction of universal primary education in 1996/97. Indeed, the development expenditure portrays the same dismal story (Table A4.3.3). The share of interest payment and loan repayment has however declined to less than 20% of the total recurrent expenditure. This has enabled government reallocate the resources that would have been used for loan repayment and interest payment to the social sector. Indeed social sector expenditures have risen since the inception of the HIPC debt initiative (Table 4.3.6).

4.3.3 Uganda's debt strategies before the HIPC Initiative

Prior to the HIPC initiative, Uganda implemented several strategies to reduce its debt burden. These debt strategies have included among others, borrowing on concessional terms, rescheduling and debt cancellation arrangements, as well as debt buyback operations. Between 1981 and 1987, the Uganda government negotiated debt rescheduling with the Paris Club creditors during which a total of US$ 184 million was rescheduled. Uganda also successfully gained access to the Enhanced Toronto terms in January 1989, under which about 30% of the eligible maturities were written off, and the maturity of the remaining debt was reduced to 14 years with an 8-year grace period. A further write-off of 50% of the outstanding maturities was obtained under the June 1992 Paris Club agreement. In July 1993, using the debt reduction facility of the World Bank, Uganda also bought back US$ 153 million of commercial debt at a substantial discount. Uganda has, over the adjustment period, also benefited from other write-offs and cancellations granted by the Paris Club countries, which led to bulk of its debt to the OECD being written-off. In 1995, Uganda also received additional debt relief from the bilateral donors, via the Multilateral Debt Fund (MDF), to help service multilateral debt obligations.

In spite of the above efforts, the external debt indicators continued to deteriorate as the country continued to accumulate debt to finance development programmes in the 1990s. By the end of 1995/96, Uganda remained heavily indebted with the external debt stock amounting to US$3.5 billion with a stock of arrears of US$250 million. The external debt-to GDP ratio was also high, averaging

about 70% between 1992/93 and 1997/98. The ratio of debt-to-export of goods also remained high although it declined from 1526.6% in 1992/93 to 535.5% in 1996/97 with the multilateral creditors accounting for 76 per cent of the Disbursed and Outstanding Debt (DOD). The debt restructuring efforts discussed above addressed creditors whose DOD was small relative to multinational creditors and as such, Uganda's debt remained unsustainable (Table A4.3.1). At the same time, the high level of multilateral debt also reduced the restructuring options that could be applied to the overall stock of DOD. The MDF and the HIPC were thus setup to substantially address the issue of multilateral debt in order to give substantial relief to countries that were pursuing prudent macroeconomic policies and to further sustain growth in these economies.

4.3.4 The HIPC Debt Relief Initiative

In 1996 the World Bank and the IMF conceived the HIPC initiative as a multi-lateral mechanism of extending debt relief to the heavily indebted poor countries that were pursuing prudent macroeconomic policies so as to reduce their debt to sustainable levels and help in sustaining good macroeconomic performance already being achieved in these economies. The key guiding principles of the initiative included additionality of debt relief, maintenance of the financial integrity of the multilateral financial institutions and burden sharing on a fair and equitable basis.

Uganda's consistency in pursuing sound policies and its commitment to structural reforms enabled it to become the first country to qualify for debt relief under the HIPC initiative. The usual three year interval between the decision and completion points was reduced to one year with a decision point set in April 1997 and the completion point reached in April 1998, when Uganda became the first country to access debt relief under the HIPC Debt Initiative. Relief was based on the ratio of Net Present Value (NPV) of debt to exports with the sustainable level of debt assessed at 202% of exports. To reach this level, the amount of relief required was $ 347 million in NPV terms which is equivalent to total saving of $650 million spread over a thirty-year period (Table 4.3.2). In the first year, 1998/99, Uganda received $45 million in debt relief and US$ 40 million was expected to be received annually for three successive years.

The first HIPC was expected to provide an '*exit strategy*' from the debt rescheduling process or, leave beneficiary countries with sustainable debt levels. Post-HIPC, a country would be expected to service its debt and still be able to direct sufficient resources to poverty reduction. However, some unforeseeable factors such as the El Nino weather phenomenon, the changes in global interest rates and the decline in international commodity prices made it difficult for Uganda to have post-HIPC sustainable debt levels. Other heavily indebted poor countries also faced varying calamities, which prevented them from achieving debt reductions to sustainable levels.

Table 4.3.2: Debt Relief under the HIPC Initiative

	Nominal debt Service Relief (millions of US$)	HIPC Debt Relief, NPV terms (millions of US$)	Decision point	Completion Point
HIPC Initiative			April 1997	April1998
Total	650	347		
Multilateral		274		
Bilateral		73		
Enhanced HIPC Initiative			February 2000	May 2000
Total	1,300	656		
Multilateral		546		
Bilateral		110		
Total HIPC Debt Relief	1,950	1,003		

Source: Ministry of Finance, Planning and Economic Development

The HIPC Debt Relief Initiative was then reformed (hence the Enhanced HIPC) to make it accessible to more countries and to deliver a deeper debt relief more quickly. The key elements of the Enhanced HIPC Initiative are:

- Lowering the debt sustainability thresholds to provide a greater safety cushion and increased prospects for permanent exit from unsustainable debt.
- Faster debt relief starting from decision points;
- Floating completion points; and
- A strong link between debt relief and poverty reduction.

In order to meet the last element of the Enhanced HIPC package, countries are expected to prepare national poverty-reduction strategies. Uganda did accomplish this, and the international financial institutions and the donor community, accepted her strategy as a viable and comprehensive one. Uganda then became the first country to benefit from the enhanced HIPC initiative in April 2000. Annual debt relief is estimated at US$ 55 million in addition to the US$ 40 million from the original initiative.

The resources from both the HIPC and the Enhanced HIPC are channeled to poverty reduction programmes through the Poverty Action Fund (PAF), which was established by the Ugandan government at the advent of the HIPC Debt Initiative. Initially, the PAF was created to ensure that resources saved from HIPC debt relief is spent on poverty reducing priority programmes. Subsequently, the PAF has attracted additional donor funding and has in practice become a mechanism for ensuring the allocation of the incremental expenditures directly to poverty reducing public services, including education, primary health care, agricultural extension, rural feeder roads, water and sanitation, and law and order. The share of the PAF in total public spending (including budget support but excluding donor projects) rose rapidly from 17% in 1997/98 to 31 % in 2000/2001. The government has pledged to continue increasing this share over time.

All PAF expenditures are an integral part of the government's budget, as envisaged by the PEAP/PRSP, which provides a framework for sector-wide plans and investment programmes, which in turn are translated into actual budgets in the

Medium-term Expenditure Framework (MTEF). The contribution of savings from HIPC debt relief to the PEAP/PRSP priority spending channeled through PAF is shown in Tables 4.3.3 and 4.3.4.

Table 4.3.3 PEAP Expenditures (billions of Ushs)

	1997/98	1998/99	1999/00	2000/01	2001/02*
Total Expenditure (Excluding arrears)	**141.38**	**231.84**	**302.69**	**439.8**	**845.5**
Of which PAF		97.84	193.98	298.8	609.3
HIPC Debt Relief		44.64	65.55	159.16	127.3
Measures to increase incomes	**8.96**	**20.39**	**31.77**	**35.79**	**65.63**
Rural Roads	8.42	20.18	24.58	28.67	42.1
Implementation of the Land Act			2.7	3.0	7.93
Agricultural Extension	0.54	0.21	4.49	4.12	15.6
Microfinance/Restocking Programmes	**0.47**	**0.49**	**7.29**	**11.64**	**12.54**
Measures to Improve Quality of Life	**128.25**	**203.28**	**251.06**	**349.96**	**459.46**
Primary Health Care	4.16	20.24	21.42	57.17	104.43
Water and sanitation	3.86	12.34	17.57	35.33	53.13
Primary Education	120.23	169.83	211.57	254.66	293.7
Other[1]	0.0	0.87	0.5	2.8	8.2
District Grants[2]	**0.0**	**0.0**	**2.0**	**24.71**	**53.28**
Monitoring and Accountability	**3.7**	**7.68**	**10.57**	**17.67**	**9.64**

Estimate; Source: Ministry of Finance, Planning and Economic development

It is therefore clearly evident that the savings from the HIPC debt relief have significantly helped in alleviating resource constraints which have enabled the Ugandan government to increase investments in poverty reducing sectors and this has contributed significantly to the poverty reduction efforts. Over the time, the PAF expenditures have been rising and estimates for 2001/02 are put at UShs.609 billion (approximately US$ 330 million)

Table 4.3.4: PEAP Expenditures (Percentage)

	1997/98	1998/99	1999/00	2000/01	2001/02*
Total Expenditure (Excluding arrears)	**100**	**100**	**100**	**100**	**100**
Of which PAF		42.2	64.1	67.9	72.1
HIPC Debt Relief		19.3	21.7	36.2	15.1
Measures to increase Incomes	**6.4**	**8.8**	**10.5**	**8.1**	**7.8**
Rural Roads	6.0	8.7	8.1	6.5	5.0
Implementation of the Land Act	0.0	0.0	0.9	0.7	1.0
Agricultural Extension	0.4	0.1	1.5	0.9	1.9
Microfinance/Restocking Programmes	0.3	0.2	2.4	2.6	1.5
Measures to Improve Quality of Life	**90.6**	**87.7**	**83**	**79.5**	**54.3**
Primary Health Care	2.9	8.7	7.1	13.0	**12.4**
Water and sanitation	2.7	5.3	5.8	8.0	6.3
Primary Education	85.0	73.3	69.9	57.9	34.7
Other[1]	0.0	0.4	0.2	0.6	1.0
District Grants[2]	**0.0**	**0.0**	**0.7**	**5.6**	**6.3**
Monitoring and Accountability	**2.6**	**3.3**	**3.5**	**4.0**	**1.2**

* Estimate; **Source:** Ministry of Finance, Planning and Economic development

4.3.5 Reforms and achievements of the Poverty Eradication Action Programme

The PEAP/PRSP has identified a set of basic services in certain poverty reducing sectors. Hence the Government has increased the share of expenditure allocated to these sectors and will continue to do so in the medium term. To this end, the government of Uganda has implemented policies aimed at:

- Creating a framework for economic growth and transformation; improving the quality of life of the poor by improving access to basic social services such as primary education, primary health care, and safe water and sanitation; increasing incomes of the poor through improving access to productive assets and information on their effective use, modernization of agriculture to improve food security and productivity, providing an adequate road network, improving rural market infrastructure and financial services, improving telecommunication and rural electrification; and promoting good governance through measures to improve security, increase transparency and accountability, decentralization, enhance flow of information, and democracy.

To date, the MTEF and the PAF have performed well in terms of containing aggregate spending within the resource envelope and delivering the desired composition of expenditure. These have enabled the government to bias public expenditure patterns towards poverty reducing social sectors and infrastructure (see Table 4.3.5). Stakeholders including donors have ensured that defense spending is kept at 2% of GDP and this has partly contributed to biasing expenditures towards poverty reducing sectors.

Table 4.3.5: Sectoral Composition of Public Expenditure
(Percentage of Total)

	1997/98	1998/99	1999/00	2000/01	2001/02
Roads and Works	4.9	6.2	8.1	8.5	8.1
Agriculture	1.1	1.0	1.5	1.5	2.2
Education	26.0	26.9	26.3	24.9	24.4
Health	6.6	6.7	6.5	7.4	8.7
Security	14.8	19.8	15.4	13.9	12.7
Water and Sanitation	0.5	1.2	1.5	2.4	2.6
Law and Order	8.9	7.2	7.3	6.5	6.5
Accountability	0.5	0.6	0.8	1.1	1.2
Economic functions, Social services and multisectoral	4.1	2.7	4.6	5.0	6.4
Public Administration	24.9	20.7	20.3	20.2	19.2
Interest Payments	7.6	7.0	7.7	8.5	8.1
All Sectors	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Ministry of Finance, Planning and Economic Development

4.3.6 Increasing the Incomes of the Poor

The policy interventions are aimed at enabling the poor, who are mainly employed in small-scale activities and agriculture, to raise their incomes through increased factor productivity. Until recently, the factor and product markets for the poor were affected by a number of factors. The 1900 Land Agreement and the Land Decree of 1975 weakened the property rights of rural households to ownership and use of land besides lowering their productivity. Absence of rural markets especially in land and labor rentals in addition to absence of extension services reduced agricultural output. Information imperfections among rural households gave rise to high levels of credit rationing where either formal on informal money market existed. As a result the capacity of the household to use recurrent inputs in agriculture as well as investment in non-farm activities was reduced and so were their incomes.

Recently, the government to date has undertaken steps to enhance the ownership of factors of production and to improve access to both factor and product markets in order to benefit the poor. Specifically, the property rights to land by the poor were addressed in the 1998 Land Act, which is expected to contribute to increased utilization and productivity of land. Productivity of labor is being addressed through policy interventions in education, health and modernizing agriculture, while access to credit to enable the poor to have increased access to factor inputs and undertake off-farm investments are continually being addressed.

4.3.7 Financial services for the Poor and Small Scale Enterprises

The poor also need accessible savings institutions in which to keep their savings. Currently, the Ugandan financial system is dominated by the banking sector whose setup cannot meet the needs of the poor. The social, cultural and economic activities of the poor in Uganda require institutions that are different from banks to service their financial needs. Indeed the experience of the last few years points to the fact that microfinance institutions (MFIs) appear most suited for this function. Unfortunately, most MFIs to date are only extending credit since the law bars them from mobilizing savings which is important for the sustainability of MFIs.

To address this problem, microfinance deposit taking institutions will be encouraged. To date, a Micro Finance Deposit taking Institutions Law has been drafted and will be tabled before Parliament in due course. Once in place, the law will facilitate soundly managed and adequately capitalized MFIs to mobilize domestic savings for on-lending to small-scale borrowers. Once the legal status of the MFIs is defined, a linkage between the banking system and MFIs is expected. Such a linkage would encourage the mobilization of savings and the retailing of credit on behalf of banks by MFIs, thereby bringing banking sector services closer to the poor.

The government is gradually withdrawing from the provision of capital for microfinance but is committed to building capacity within the MFIs. In particular, the

Poverty Alleviation Project (PAP) has secured funding of US$ 20 million over the next five years for capacity building in a broad sense; and for on-lending by NGOs and private sector operators. There are also plans to set up a capacity-building fund from which MFIs, that perform well on social and financial criteria, can draw.

The government also recognizes the important role that micro credit plays in the Programme for Modernization Agriculture in supporting income-generating activities, particularly in rural areas. The Rural Micro Finance Support Programme (RMSP) has been designed and made operational with funding from the African Development Bank (ADB). The RMSP funds will be channeled through independent MFIs operating at the grassroots level, which will be responsible for delivering and recovering the credit.

4.3.8 Uganda's experience with Small and Medium-Scale Enterprises (SMEs)

SMEs in Uganda have increasingly become important vehicles of economic growth, development and poverty reduction through their contribution to the creation of wealth, employment and income generation. In spite of their importance however, SMEs suffer from constraints that lower their resilience to risk thus preventing them from growing and attaining economies of scale. These inherent weaknesses also make it difficult for SMEs to access credit from the formal financial sector. In recognition of their important role in fostering growth and development, and the constraints that befall them, the government has put in place a number of programmes to support SMEs.

1. Credit programmes to support SMEs

The Bank of Uganda (BOU) operates a number of credit schemes on behalf of itself, the government and the donors. These credit schemes provide loans to small and medium size enterprises in the private sector through licensed banks. The credit schemes currently in operation include:

- Apex Private Sector Loan Scheme, which is designed to support small and medium-sized private sector enterprises in manufacturing, agro-processing, and services, including tourism.
- Export Refinance Fund (ERF), which is designed to provide working capital to support small and medium size enterprises engaged in non-traditional exports.
- Distressed Flower Project Fund (DFPF), which was established to rescue flower firms recently found to be facing some distress especially with regard to working capital and replacement of green houses.

Other credit schemes administered by the Bank of Uganda in the past included the Export Promotion Fund (EPF), the Development Finance Fund (DFF), the Investment Term Credit Refinance Fund (ITCRF), the Cotton Sub-Sector Development Project (CSDP), and the Rehabilitation of Public Enterprises (RPE) project.

2. Other BOU support programmes for SMEs

In addition to the above schemes, support programs for building the capacity of financial institutions intermediating resources to SMEs have also been undertaken. The Support Programmes currently in operation include the following:

- Export Credit Guarantee Scheme launched in December, 2000 to support the export of non-traditional products originating from Uganda with 35% Ugandan content.
- African Rural and Agricultural Credit Association (AFRACA), which fosters co-operation between government and financial institutions in the field of agricultural credit and banking.
- DANIDA funded Rural Financial Services Component (RFSC); and
- Capacity Building Programme (CBP), which wound up in December 2000, was established purposely to build the capacity of micro-finance institutions in rural areas to enhance their capacity to deliver rural financial services.

3. Performance of the BOU support schemes

Aggregate data on overall performance of SMEs is lacking. However, based on the performance of SMEs supported by BOU, there is evidence pointing to the success of most of these SMEs. The DFPF has, for example, revitalized the flower exports with export values rising from US$ 5.3 million in 1996/97 to US$ 16.4 million in 2001/02 and are projected to rise even further in the subsequent years as shown in table 4.3.6. Maize exports have also risen largely on account of the Uganda Grain Exporters Association (UGEA- an association that brings together SMEs involved in grain exports) being able to access financing for maize exports from commercial banks' with the financial guarantee from BOU. Prior to the UGEA initiative, the price of maize grain in the rural areas had fallen to as low as USH. 30 (US$0.02) per kilogram. Since then, the price has gradually risen to USH. 100 (US$ 0.06). This on its own has raised the incomes of the rural poor in addition to more than doubling maize export receipts in 2001/2. A number of SMEs engaged in fish exports have also accessed financing through BOU and this together with the lifting of the ban on fish exports to the European Union (EU) helped in raising the value of fish exports by more than 60 per cent in 2001/2.

As seen in Table 4.3.6, growth is projected in export earnings over the medium term largely as a result of alleviation of constraints including financing, that the SMEs face. Based on the performance of the SMEs supported by BOU, one could argue that their contribution to employment and GDP have been positive although actual data to back this is still lacking.

Table 4.3.6 Performance of selected Non-Traditional Exports (millions of US$)

	1995/96	1996/97	1997/98	1998/99	1999/00	2000/1	2001/2	2002/3*	2003/4*
Flower	5.4	5.3	6.8	7.2	8.3	13.2	16.4	19.6	23.6
Maize	9.43	16.53	8.08	5.89	4.01	6.13	14.84	15.42	21.09
Fish	37.6	34.6	28.0	47.6	18.6	50.1	87.5	119.7	130.0

* Projection; **Source:** Bank of Uganda

3. Support Institutions for SMEs

Currently, a number of support institutions for SMEs exist and these have various roles as outlined below.

- Private Sector Foundation (PSF) which is an advocacy body for member private sector associations. It also administers the Business Uganda Development Scheme (BUDS).
- Uganda Manufactures Association (UMA), which is an umbrella association for manufacturing establishments. This helps coordinate the activities of its members.
- Uganda Investment Authority (UIA), which is a one-stop-centre for investors. The UIA helps facilitate investment activities in the country.
- Uganda National Chamber of Commerce and Industry (UNCCI) is an advocacy organization for enterprises involved in trade and manufacturing.
- Uganda Export Promotion Board (UEPB) was established to provide exporters with a wide range of services, which inter-alia, include: providing assistance in overseas marketing and national export promotional activities; providing market information services; providing regular training services to exporters and trade officials in all trade related disciplines.
- Uganda Small Scale Industries Association (USSIA), which is an advocacy group for small and micro enterprises helps co-ordinate the activities of its members.

The government has supported the activities of the above institutions so as to facilitate the development of SMEs.

4. Challenges currently faced by SMEs in Uganda

- There is need for continued capacity building in SMEs so as to improve on their corporate governance. This is crucial especially in the area of proper financial records and modern management techniques, which are necessary for sustainability.
- To be able to meet the challenges of competition, there is need for vertical and horizontal integration of SMEs. This will enable then build linkages with other entrepreneurs and acquire raw materials, skills and expertise that they need.
- Accessing credit from the formal financial institutions is still problematic. Those that have succeeded have done so only because they either have a track record or have been guaranteed by BOU. A majority of young SMEs

are faced with the problem of credit access since they do not have any track record besides getting a guarantor is not yet as easy for them.

4.3.9 Lessons from the Ugandan experience

Evidence on private consumption from five recent Ugandan household surveys shows that the number of people living below the poverty line has fallen from 56 per cent in 1992 to 35 per cent in 2001. The reduction in poverty is explained mainly by economic growth, and partly through falling income inequality. Evidence provided in Deininger et. al. (2001) shows that imperfections in both factor and product markets generally reduced, resulting into increased agricultural output and productivity by the poor rural households during the period 1990-1999. This is mainly attributed to the poverty reduction strategies and the trade liberalization policies being pursued by the government. Policies that strengthened the property rights to resources already owned by the poor enhanced their asset position and had a significant impact on the functioning of the factor market. Critical is the involvement of the poor in the overall growth process by means that increases their access to productive resources and enhances their productivity in a market friendly environment. This is also necessary in sustaining economic growth while addressing income inequality among people, sectors and regions.

However, the sustainability of this poverty reduction is of concern as most of it happened during the coffee boom which, has since unwound. In addition, the impressive growth rates generated from increased capacity utilization resulting from the rehabilitation of the existing productive capacity and pursuance of prudent macroeconomic policies are unlikely to be sustained in the future without a higher share of investment and continued export growth and diversification. This is the motivation for increased investment in human capital and poverty reducing sectors financed by HIPC Initiatives discussed above.

1. HIPC Debt Initiative and Poverty Reduction

The Ugandan experience with the HIPC initiative provides a number of policy lessons for countries in similar situations. Four key components are identified in these policies:

- Prudent macroeconomic policies, which include monetary, fiscal and exchange rate policies to provide a stable environment for economic activity to take place besides being a necessary condition for poverty reduction.

- Structural policies to create good incentives for accumulation of wealth by households and firms by pursuing prudent trade, tax and sectoral policies.

- Public sector management to provide services which complement the private sector. Specifically, efforts to build sustainable capacity in government to deliver social services and strengthen property rights, rule of the law and rehabilitation of physical infrastructure are essential thus making

good governance and security indispensable. This has the impact of laying ground for increasing absorption capacities for future delivery of resources.

- Social inclusion policies, which ensure full participation of society in social services that benefit the poor and the marginalised groups, are necessary. One key lesson in this area is that involvement of all stakeholders improves service delivery and monitoring mechanisms. Consequently, the role of NGOs and Civil Society Organizations (CSOs) in the fight against poverty is important.

- Capacity building in debt management is necessary if the debt problems are to be minimized. A considerable part the problem in Uganda's external debt was due to lack of technical capacity. There is, therefore, need to strengthen debt management capabilities and debt coordination..

2. Small and Medium-scale Enterprises (SMEs)

The Ugandan experience with SMEs reveals the following:

- A stable macroeconomic environment is necessary for the profitability and the sustainability of SMEs. By helping in the creation of wealth, employment, and income, they have had an important role in the fight against poverty.
- Finance plays a critical role in the growth, development and sustainability of SMEs and yet SMEs usually experience difficulties in accessing loans from the banking system. Credit guarantees for viable SMEs without credit track record but with bankable projects should be supported at lease in the short-run.
- SMEs need special support programmes to help them build capacity and improve on their corporate image. Capacity building is important if professionalism and efficiency in the management of SMEs is to be enhanced. Special institutions to co-ordinate the activities of SMEs are also important.

The effectiveness of these policies issues, particularly the HIPIC debt relief, the microfinance and SMEs, will further be discussed in Chapter V.

V. RESOURCE FOR FINANCING DEVELOPMENT: EXPERIENCE OF THE FACILITATING MULTILATERAL INSTITUTIONS

5.1 Introduction

The great challenge facing much of the developing countries is to mobilize adequate resources to promote poverty-reducing growth and see the burden of poverty and its miseries reduced. Certainly, attaining poverty reduction sustainability requires considerable resources and creative utilization of the existing ones. Given the weakening global growth, falling commodity prices, increased refugee flows, and the existing significant barriers to the exports of developing countries, the need and stake were never greater. In economies that stall or fall into recession, the number of people living on less than $1 per day will actually increase. Moreover, the volatility of private capital flows has created additional problems for resource-constrained, commodity-dependent low-income countries. Indeed, the actions of developing countries are paramount in determining the progress in the process of mitigating resource constraints. However, concerted efforts by both developed and developing world are needed if the goal of alleviating poverty has to be achieved. In this environment, it is particularly important for multilateral institutions to explore any opportunity to facilitate resource mobilization to resource-constrained countries.

Realizing the large resource gaps in the Least Developing Countries (LDCs) and their urgent needs for sustained growth and development, multilateral institutions are currently working with donor governments in helping these countries find ways to spur growth and empower poor people. In particular, the multinational institutions and donor countries are trying to learn from past experiences by reshaping the allocation, design, and delivery of programs to countries with weak institutions, governance and policies. More specifically, the multinational institutions are looking for effective ways of helping poor countries overcome their resource constraints and respond to the challenges of poverty. This rethinking is a response to two major trends of the 1990s. The first comprises globalization and liberalization. The second is the uneven distribution of the costs and benefits of these processes.

In supporting the aim of the study, this chapter presents a comprehensive record of the flow of ideas, policies, and programs that enhance the flow of external[1] financing to mitigate the resource constraints in LDMC. We further discuss strategies for mobilizing domestic resources before drawing broad lessons about ways to enhance the effectiveness of the policy stance adopted by IDB member countries.

To this end, the following policies and programs are perceived to be the main vehicles used by the IMF, the World Bank, and other multilateral institutions to mitigate resource constraints and provide support to the low-income countries.

5.2 Using Official Development Assistance (ODA) to Mitigate Resource Constraints in Poor Countries

One of the vehicles used by the multilateral institutions and donor countries to help mitigate resource constraints in least developing countries is official development assistance (ODA) or aid; consisting of grants, loans, or technical cooperation. Over the last 50 years or so, developing countries depended largely on foreign aid to relax their resource constraints and promote sustained poverty-reducing growth[2]. Substantial amounts of aid were disbursed for low-income countries under the assumption that aid would supplement domestic savings, creating conditions for poor people to raise their incomes, live longer, healthier and lead more productive lives. While earlier empirical studies consistently found a weak relationship between aid and investment, and for that matter growth, more recent research shows that aid makes an effective contribution to growth and poverty reduction in countries with good economic policies, sound institutions, and strong governance. In places were aid was complemented by sound policies, countries have achieved impressive growth rates. Consequently, since 1990 the share of people living in extreme poverty in developing countries has dropped from 29 percent to 23 percent (Global Development Finance, 2002). Yet, in much of the developing world where policy was weak, growth slowed, external debt mounted, and in some places such as Sub-Saharan Africa (SSA), living standards stagnated or declined; contributing to the perception that aid flows have failed to support development. As a caveat, it is worthy to mention here also, like all economic inputs, ODA is subject to diminishing returns. Perhaps even countries with excellent policies and sound institutions are limited in their capacity to absorb much aid.

This mixed progress in aid outcomes has led to the revision and reconsideration of aid policies and strategies. In order to make ODA more effective in financing development and to raise the marginal productivity of aid, a radical rethinking of international development cooperation is now under way. Concerted efforts by multilateral institutions, donors and national governments were directed to promote growth and fight poverty in LDCs under new terms of cooperation and partnership (Box 5.1).

The multilateral institutions are coordinating with the developed countries to increase the ODA and improve its effectiveness, including aligning it fully with country-led strategies for mobilizing domestic resources[3]. Emerging evidence suggests that assistance works and could be sustained when the recipients are implementing desirable policies and the process is owned by them (World Bank, 2002). In countries where poor public policy dominates, aid can harm the very citizens it is meant to help; crowding out private investment and perpetuating failed policies. Meanwhile, the mid-1990s saw a sharp decline in bilateral foreign aid despite the commitments made in The 1992 World Summit on Sustainable Development, (Table A5.1 and Table A5.2). Between 1996 and 2000, ODA decreased from US$14.42 billion to US$12.76 billion for LDCs, and from US$19.37

billion to US$12.98 billion for developing countries. The amount of ODA provided by donors fell by 1.6 percent in real terms in 2000 to $53.1 billion, or 0.22 percent of the Development Assistance Committee (DAC) members' GDP (data on aid flows from donors for 2001 are not yet available). The 1990s also witnessed some reluctance from the governments of rich countries to increase the direct lending capacity of the multilateral institutions (see, Bird and Rowlands, 2001).

Box 5.1: The New partnership for Africa's Development (NEPAD)

The New Partnership for Africa's Development (NEPAD) is a pledge by all of Africa's leaders to eradicate poverty and move towards sustainable growth and development. The partnership focuses on African ownership of the development process and seeks to reinvigorate the continent in all areas of human activity. Through the partnership, African leaders have agreed to:

- Strengthen mechanisms for conflict prevention, management, and resolution.
- Promote and protect democracy and human rights by developing standards for Accountability, transparency, and participatory governance.
- Restore and maintain macroeconomic stability.
- Implement transparent legal and regulatory frameworks for financial markets.
- Revitalize and extend education, technical training, and health care services.
- Promote women's role in social and economic development.
- Promote the development of infrastructure, agriculture, agroprocessing, and manufacturing to meet the needs of export and domestic markets and local employment.

The NEPAD document draws African's attention to the seriousness of the continent's economic challenges, the potential for addressing them, and local mobilizing support for change. The main strategies proposed include:

- Fostering conditions for long-term peace, security, democracy, and good governance by, among other things, building capacity for early warning systems, addressing political and social vulnerabilities, combating the illicit proliferation of small arms and light weapons, and implementing institutional reforms of public services.
- Promoting the provision of regional and subregional public goods such as water, transportation, energy, environmental management, and other infrastructure-notably telecommunications.
- Developing education and human resources at all levels, and particular increasing the role of information and communication technology in education and training, inducing a "brain gain" for Africa, and eliminating gender disparities in education.
- Increasing domestic resource mobilization and accelerating foreign investment.
- Creating a conducive environment for private sector activities, with an emphasis on domestic entrepreneurs.
- Promoting the inflow and effective use of official development assistance (to support the provision of international public goods in Africa) by reforming systems for delivering and evaluating aid.
- Pursuing gender equality in education, business, and public service.
- Supporting efforts by the Economic Commission for Africa to strengthen Poverty Reduction Strategy Paper Learning Groups.

Source: Economic Commission for Africa (official sources).

Nonetheless, since 1980s, the World Bank has moved into the area of policy-based lending via its structural and sectoral adjustment programs. In countries committed to reforms, the World Bank adjustment operations have

contributed to macroeconomic stability and the removal of key economic distortions. Lessons learned from both the World Bank experience and from research show that there is a strong relationship between development and ODA. Despite some failures and shortcomings, the ODA has often helped to underpin and support success and is becoming more effective in doing so (see, *The Role and Effectiveness of Development Assistance: Lessons from World Bank Experience, 2002*). It is strongly asserted by the World Bank and other multilateral institutions that support to developing countries should be based on country owned poverty reduction strategies, whereby the actions of developing countries are paramount in determining progress in the fight against poverty. According to the IMF/World Bank, international support for development will have only limited effects if governments in developing countries do not share the commitment to poverty reduction. Well-designed development strategies, as well as reforms to policies, institutions, and governance are needed if international assistance has to materialize.

To help the least developing countries mitigate their resource constraints, the World Bank assistance broadly comes in two forms: project and program lending. The two broad categories consist of technical assistance (TA), highly concessional loans through the International Development Association (IDA), and participation loans to the private sector through International Financial Corporation (IFC). In addition, the World Bank's existing instruments and policies make available a wide variety of options to provide financial assistance to resource-constrained countries affected by the economic downturn and the September 11 events and their aftermath-including both new lending and disbursements under the existing loans (Box 5.1). IDA, IFC, and MIGA will use these options to respond flexibly in helping countries meet their financial needs and supporting sound poverty reduction strategies and social programs. The Bank also has the flexibility, within the existing policies, to work with borrowers to restructure the existing portfolios. For example, by reallocating loan proceeds to channel resources to activities that most effectively mitigate the resource constraints, or to increase and accelerate disbursements under the existing options (World Bank-IMF Joint Statement, 2001). In this regard, the IDA projected lending for FY02 is up to $7.8 billion, compared with up to $7 billion before September 11 events. Beyond the current fiscal year, the initial estimate of lending during the IDA 13 period (FY02-FY05) was $23 billion (SDR 18 billion). Estimates completed after September 11 events suggest that the crisis and ongoing economic downturn could result in significant incremental needs during IDA 13, particularly for countries in Africa.

On the other hand, the IMF's volume of loans to low income countries has fluctuated significantly over time. The oil shock of the 1970s and the debt crisis of the 1980s were both followed by sharp increases in IMF lending. In the 1990s, the transition process in Central and Eastern Europe and the crises in emerging market economies led to another surge in the demand for IMF resources.

Over the years, the IMF has developed a number of loan instruments, or "facilities", that are tailored to address the specific circumstances of its diverse membership (Box 5.2). Currently, the IMF provides assistance to low-income

countries in two ways: through concessional lending under the Poverty Reduction Growth Facility (PRGF) and through debt relief under the Heavily Indebted Poor Countries (HIPC) Initiative. In September 1999, the IMF broadened its concessional lending to include an explicit focus on poverty reduction in the context of a growth-oriented strategy. According to a recent joint statement of the President of the World Bank and the IMF Managing Director, the two institutions would support strategies elaborated by the borrowing country in a Poverty Reduction Strategy Paper (PRSP) prepared with the participation of civil society—including the poor—and other development partners. Reflecting the new objectives and procedures, the IMF established the Poverty Reduction and Growth Facility (PRGF), which will be based on the PRSP, to replace the Enhanced Structural Adjustment Facility (ESAF).

Except for the PRGF, all facilities are subject to the IMF's market-related interest rate, known as the "rate of charge", and some carry an interest rate premium, a "surcharge". The rate of charge is currently about 2.7 percent. The IMF discourages excessive use of its resources by imposing a surcharge on large loans, and countries are expected to repay loans early if their external position allows them to do so. According to the IMF's projections, the demand for PRGF resources is expected to be as much as $1.5-2.0 billion for the FY02. Meanwhile, the minimum resources necessary for continuation of PRGF lending has been secured with the contribution of SDR 4.1 billion to the PRGF Trust by nine lenders(see Box 5.1).

5.3 HIPCs' Debt Relief and Resource Constraints

In 1996, the World bank and the International Monetary Fund (IMF) jointly launched the Highly Indebted Poor Countries (HIPC) Initiative with the aim of helping these countries mitigate resource constraints and reduce the foreign debt to sustainable levels in a reasonably short period (Box 5.3). The implementation of the Initiative is expected to help governments focus on policies and reforms that are necessary for the simultaneous achievement of sustainability, sustained growth and poverty reduction. The original HIPC framework was based on four building blocks: First, *eligibility*-restricted to IDA and Enhanced Structural Adjustment Facility (ESAF) countries, with strong track record of performance under the IMF/World Bank supported programs, who are not expected to achieve debt sustainability with traditional debt-relief mechanisms. Second, *debt sustainability* analysis (DSA)-at the decision point by IMF/World Bank staff after full consideration of vulnerability indicators. The key indicator of external debt sustainability is the ratio of the net present value (NPV) of debt to export. Third, *performance criteria*-to be met during the second stage to qualify for support under the initiative, including macroeconomic indicators and progress on structural and social reforms. Fourth, *participation*- of all relevant creditors and the country concerned. Moreover, implementation of the HIPC involve a "decision point" to be reached when the eligible country establishes a 3 year track record of strong policy performance demonstrating that it is in a position to use the additional resources effectively. Further, the qualifying country has to continue implementing macroeconomic reforms and structural adjustment policies (supported by

concessional lending from the IMF and World Bank) for a further period of three years to reach "completion point," which would trigger the irrevocable granting of debt relief.

Box 5.2 IMF Facilities

Poverty Reduction and Growth Facility (PRGF). The IMF for many years provided assistance to low-income countries through the Enhanced Structural Adjustment Facility (ESAF). In 1999, however, a decision was made to strengthen the focus on poverty, and the ESAF was replaced by the PRGF. Loans under the PRGF are based on a Poverty Reduction Strategy Paper (PRSP), which is prepared by the country in cooperation with civil society and other development partners, in particular the World Bank. The interest rate levied on PRGF loans is only 0.5 percent, and loans are to be repaid over a period of 5½–10 years.

Stand-By Arrangements (SBA). The SBA is designed to address short-term balance-of-payments problems and is the most widely used facility of the IMF. The length of a SBA is typically 12 –18 months. Repayment is normally expected within 2¼–4 years unless an extension is approved. Surcharges apply to high levels of access.

Extended Fund Facility (EFF). This facility was established in 1974 to help countries address more protracted balance-of-payments problems with roots in the structure of the economy. Arrangements under the EFF are thus longer (3 years). Repayment is normally expected within 4½–7 years unless an extension is approved. Surcharges apply to high levels of access.

Supplemental Reserve Facility (SRF). The SRF was introduced in 1997 to meet a need for very short-term financing on a large scale. The sudden loss of market confidence experienced by emerging market economies in the 1990s led to massive outflows of capital, which required loans on a much larger scale than anything the IMF had previously been asked to provide. Countries are expected to repay loans within 1 –1½ year, but may request an extension by up to 1 year. All SRF loans carry a substantial surcharge of 3 –5 percentage points.

Contingent Credit Lines (CCL). The CCL differs from other IMF facilities in that it aims to help members prevent crises. Established in 1999, it is designed for countries implementing sound economic policies, which may find themselves threatened by a crisis elsewhere in the world economy—a phenomenon known as "financial contagion". The CCL is subject to the same repayment conditions as the SRF, but carries a smaller surcharge of 1½–3½ percentage points.

Compensatory Financing Facility (CFF). The CFF was established in the 1960s to assist countries experiencing either a sudden shortfall in export earnings or an increase in the cost of cereal imports caused by fluctuating world commodity prices. The financial terms are the same as those applying to the SBA, except that CFF loans carry no surcharge.

Emergency assistance. The IMF provides emergency assistance to countries that have experienced a natural disaster or are emerging from conflict. Emergency loans are subject to the basic rate of charge and must be repaid within 3¼–5 years.

Source: IMF, 2001

In late 1999 the Enhanced HIPC Initiative was endorsed incorporating lower targets and thresholds, modified performance requirements, and strengthening the link between debt relief and poverty reduction through comprehensive development strategies described in Poverty Reduction Strategy Papers (PRSPs). The PRSPs have to be prepared by countries eligible for aid through a country-driven broad-based participatory process involving civil society organizations and other stakeholders[4]. Under the Enhanced HIPC, there are now a total of 26 countries that have reached decision points (12 of them are IDB members), qualifying for debt service relief amounting to some $36 billion.

Enhancement to the HIPC Initiative to provide deeper, broader, and faster debt relief increased substantially the cost of the Initiative. The total cost of the enhanced HIPC framework is estimated at US$34.4 billion in end-2000 NPV terms, or US$36.4 billion in 2001 NPV terms. The IMF is estimated to contribute US$2.7 billion in 2001 NPV terms, and the World Bank's share of financing is expected to increase to US$8.1 billion in 2001 NPV terms (IDA/SecM2002-0155 document, March 22, 2002).

Box 5.3 The Highly Indebted Poor Countries (HIPC) Debt Relief Initiative

Efforts to deepen debt relief for poor countries suffering from unsustainable debt burdens culminated in the Highly Indebted Poor Countries (HIPC) Initiative, launched in 1996. This initiative aims to increase the effectiveness of aid by helping poor countries achieve sustainable levels of debt while strengthening the link between debt relief and strong policy performance. Forty-two countries, primarily from the Sub-Saharan Africa region, are identified as eligible to receive debt relief under this initiative. In 1999 the scope of the initiative was widened to accelerate and deepen the provision of debt relief. As of December 2001, 24 countries have reached the decision point 1 (the point where debt relief is approved by the Executive Boards of the IMF and the World Bank, and interim relief begins). These countries are now receiving debt service relief that will amount to about $36 billion over time, with a $21 billion reduction in the present value of their outstanding debt stock. For the 24 countries that have reached their decision points, HIPC alone has reduced the present value of external debt by about half. When combined with other debt reduction mechanisms, this implies a two-thirds reduction in these countries' external indebtedness. Not only does HIPC reduce debt overhang, but it also supports positive change toward better poverty reduction. Debt relief under the HIPC Initiative is intended for countries that are pursuing effective poverty reduction strategies, and both better public expenditure management and increased social expenditures are critical elements of this. For the countries that have reached decision points under the HIPC Initiative, the ratio of social expenditures to GDP is projected to increase from 5.8 to 6.9 percent between 1998–99 and 2001–03. The challenge is to ensure that these expenditures translate into better social-sector outcomes, and more importantly that the broader policy environment continues to improve and support growth and poverty reduction.
Source: World bank 2002

There has already been a significant reduction in debt stock and debt service in the HIPC countries. Thus far, the IMF has already committed enhanced HIPC Initiative assistance of US$1.7 billion to 22 of its member countries; 12 of which are IDB member countries (see Table 5.1 below). The total assistance from all creditors to these countries will reduce their external debt stock by US$20 billion in NPV terms, or by nearly one-half. In combination with traditional debt relief and pledges of additional bilateral forgiveness, the external indebtedness of these 22 countries will be reduce by about two thirds or from US$53 billion to US$20 billion in NPV terms.

Since 12 of the HIPC-eligible countries are LDMCs, the HIPC Initiative can play an integral part in alleviating the resource constraints problem experienced by these countries. As discussed in chapter IV, funds released from debt relief can be used in poverty reduction programs such as health and education. Table 5.1 shows the amount of debt relief committed to the 12-HIPC IDB member countries totaled US$625.8 million. More than 50 percent of this amount, or US$385.2, is already disbursed.

Table 5.1 Commitments and Disbursements of IMF HIPC Initiative Assistance to IDB Member Countries (As of end-March 2001)

Member Countries	Decision Point	Completion Point	Amount Committed	Amount Disbursed	Amount Committed	Amount Disbursed
			(In millions of SDRs)		(In millions of US$)	
Benin	Jul. 2000	Floating	18.4	3.7	24..3	4.9
Burkina Faso	Sep. 1997	Jul. 2000	16.3	16.3	21.7	21.7
Burkina Faso	Jul. 2000	Floating	15.0	1.5	19.9	2.0
Cameroon	Oct. 2000	Floating	28.5	2.2	36.9	2.9
Gambia, The	Dec. 2000	Floating	1.8	0.1	2.3	0.1
Guinea	Dec. 2000	Floating	24.2	2.4	31.4	3.1
Guinea Bissau	Dec. 2000	Floating	9.2	0.5	11.9	0.7
Mali	Sep. 1998	Sep. 2000	10.8	10.8	14.0	14.0
Mali	Sep. 2000	Floating	33.6	0.7	43.7	0.9
Mauritania	Feb. 2000	Floating	34.8	9.9	46.8	13.3
Mozambique	Apr. 1998	Jun. 1999	93.2	93.2	124.6	124.6
Mozambique	Apr. 2000	Floating	11.6	2.3	15.6	3.1
Niger	Dec. 2000	Floating	21.6	0.4	27.8	0.6
Senegal	Jun. 2000	Floating	33.8	4.8	45.0	6.4
Uganda	Apr. 1997	Apr. 1998	51.5	51.5	68.9	68.9
Uganda	Feb. 2000	May 2000	68.1	68.1	91.0	91.0
Total			472.4	268.4	625.8	385

Source: www.imf.org/external/np/tre/finasst/2001/042001.htm

5.4 Building Capacity to Mitigate Resource Constraints

Most of the poor countries lack the resources and the professional standards to strengthen their institutions and implement the structural reforms needed to overhaul their economies. In effect, they face severe financial and physical constraints. Meanwhile, the economic and structural reforms indispensable for many developing countries require strengthening of domestic institutional and administrative capacities. Most important, capacity building programs will continue to be stressed in countries implementing adjustment reforms supported by the IMF's PRGF and the World Bank's IDA. In this context, both the World Bank and the IMF are responding to the needs of the low-income member countries by updating the diagnostics, strengthening capacity and increasing technical assistance. In many countries, technical assistance focuses on areas such as trade policy, fiscal and public expenditure management (see Box 5.4), financial management and procurement reform, financial sector reform, and the design and implementation of social safety nets, including targeting of pro-poor spending[5].

Indeed, the World Bank, IMF, IFC and other organizations have launched various capacity-building programs in the low-income countries to strengthen governmental capacity to plan and implement poverty reduction actions. In effect, these capacity buildings efforts help mitigate the resource constraints in two ways. First, they improve human development by enhancing skills and fostering the

technical know-how required for the success of pro-poor growth. Second, they build institutions and release some highly needed financial resources to be used to in poverty-reduction programs.

An important area of capacity building in low-income countries is governance and leadership reforms. Because governance goes to the heart of how power is exercised, how decisions are made, and how government interacts with citizens, the World Bank treated "good governance" as something to be "installed" in a poor country, much as an infrastructure project might install a bridge or a power dam. The World Bank is with the view that, in a dysfunctional governance environment, public administration capacity is underused and not oriented toward economic and social development. Consequently, the World Bank has started governance-supported programs to reform the public administrations and build local capacity in Sub-Saharan African countries since the 1980s. The efforts, which started as an adjunct to structural adjustment lending, led to a strong bias toward reducing the size and cost of African public administrations- a focus on efficiency rather than effectiveness. After two decades of governance support in Sub-Saharan Africa, the blueprint approach to reform failed (Schacter, 2000). An emerging lesson is that the dearth of local capacity is not only a cause but also a consequence of poor governance and failed approaches to governance support. If reforms are to have a reasonable chance of success, they must pay careful attention to the quality of local leadership for reforms; local capacity to design and implement reforms; and capacity-building needs of decentralized as well as centralized forms of governance (Box 5.4). Another capacity building program that is closely related to governance reform and emphasized by the World Bank and IMF, is public expenditure management (PEM). The PEM provides TA on revising and prioritizing the budgetary process, cleaning the development budget, shifting resources toward areas where the poor are, and introduce civil society monitoring (Box 5.3).

Recently, the African Development Bank (ADB) and the African Development Fund (ADF), collaborated with the Governments of four Nordic countries (Denmark, Finland, Norway, and Sweden) to sign an agreement that made available to the ADB an US $ 1.0 million to establish the Nordic Trust Fund for Governance. According to ADB, the amount will be used to fund activities to promote good governance in ADB Regional Member Countries (RMCs) and activities that endeavor to mainstream good governance into the Bank's operations. These activities would primarily be based on RMCs' national development plans and poverty reduction strategies as well as the ADB Group's Policy on Good Governance. The resources of the Trust Fund will also be utilized to co-finance activities with other partners such as bilateral donors, the Bretton Woods institutions and UN Specialized Agencies. Furthermore, the activities must include measures to combat corruption, create credible audit and oversight institutions to deepen the reforms of public administration and promote sound public financial management.

Box 5. 4 World Bank/IMF Ongoing PEM Work

The World Bank has a number of programs and projects in HIPCs which incorporate elements of capacity building in Public Expenditure Management (PEM) systems, whether at the center of government (e.g., ministry of finance) or in sectors (e.g., health, transportation). This includes adjustment and technical assistance (TA) loans (e.g., to reform public policies in the expenditure area, to assist in building a MTEF, to introduce external audit and civil society monitoring, or to finance and oversee the installation of computerized information systems) and Economic and Sector Work (ESW) such as Public Expenditure Reviews (PERs), often with related public expenditure tracking or incidence surveys; Country Financial Accountability Assessments (CFAAs); Country Procurement Assessment Reviews (CPARs); and Institutional and Governance Reviews (IGRs). In the aggregate, approximately $3 billion of the World Bank's adjustment lending in both FY99 and FY00 contained conditions regarding public expenditure management reform, and about $250 million of investment lending in each year was designed to provide TA in public expenditure management. About 20 to 30 PERs, CFAAs, and CPARs each are completed annually. The public expenditure tracking survey (PETS), a relatively new World Bank analytic instrument, is particularly appropriate for addressing some short-term HIPC expenditure tracking issues. Five PETSs were recently undertaken in 4 countries, with more planned in several HIPC countries. Their detailed implementation can be adjusted to give more priority to reforms that will enable tracking of poverty-reducing spending. In particular, the new Poverty Reduction Strategy Credits (PRSCs) can target specific aspects of the PEM process.

IMF technical assistance has been delivered through a combination of missions and resident or peripatetic experts. From 1995–2000, FAD undertook 20 such missions, all of which provided reports to countries setting out recommendations for reforms. In addition, over this period, there were between 4 and 9 resident advisors in these countries. Currently, the IMF has a total of 8 resident PEM experts in HIPCs, whose terms of reference can be adjusted to include some of the changes required to ensure satisfactory tracking. IMF TA, including work to strengthen tracking capacity, can be provided as follow-up to completion of the fiscal module of the Reports on Observance of Standards and Codes (ROSC): 8 such ROSCs are planned in HIPCs over the next 6 months.

The World Bank and the IMF should also build on regional efforts directed at strengthening PEM capacity, such as implementation of budget classification standards mandated by the West African Economic and Monetary Union (UEMOA).

Source: World Bank 2001.

The IMF technical assistance programs cover a broad range of macroeconomic policies, fiscal policy, monetary policy, management and statistics. Specifically, the IMF assistance falls in three broad areas: (a) design and implementation of fiscal and monetary policies; (b) institution building, such as the development of central banks, treasuries, tax and customs departments, and statistical services; and (c) drafting and review of economic and financial legislation[6]. Currently, about three-quarters of IMF technical assistance goes to low and lower-middle income countries. For example, the IMF Institute channels a significant share of its training resources into cooperation with regional training institutes in Africa (such as the one in Dakar). The Fund also organizes high-level seminars that bring together senior officials of African governments to exchange views on policy issues of special relevance to the region, in line with African Governors' demand for the promotion of regional "centers of excellence" (Box 5.5).

Box 5.5 Domestic Capacity Building in Africa

One capacity-building effort that has paid significant dividends is the African Economic Research Consortium (AERC), which was established in 1988 as a research institute and now covers 22 countries. Its secretariat is located in Nairobi. The AERC works to strengthen local capacity for conducting rigorous, independent inquiry into issues affecting economies in Sub-Saharan Africa.

The AERC focuses on improving economic policy through research, training, and dissemination of research findings. The AERC conducts research in-house and administers a small grants program for researchers in academia and policymaking institutions. The AERC has supported 280 research projects, and the number of participating researchers has grown from 40 to 200 since its inception. Encouraged by this success, the Executive Board of the International Monetary Fund (IMF) endorsed the IMF's Africa Capacity Building Initiative. The Initiative is part of the IMF's response to the urgent call by African leaders, included under the New Partnership for Africa's Development (NEPAD), to strengthen economic governance and domestic capacity of governments to carry out sound economic poverty-reducing policies. The Initiative's strategic goal is to strengthen the capacity of African countries to design and implement their poverty-reducing strategies, as well as to improve the coordination of capacity building technical assistance in the Poverty Reduction Strategy Paper (PRSP) process. The Initiative aims to increase the volume of capacity building assistance from the IMF to Africa in the IMF's core areas of expertise.

As part of the Initiative, the IMF signed agreements to establish African Regional Technical Assistance Centers (AFRITACs), in Dar es Salaam and Abidjan. The two centers will assist countries in East and West Africa to build local capacity for economic and financial management. Through the centers, the IMF will provide assistance with a team of resident experts, supplemented by short-term specialists, as well as through in-country workshops, professional training and regional courses. Training and technical assistance from the AFRITACs will concentrate on the IMF's core areas of expertise in close cooperation with the World Bank, the African Development Bank, and donors. An independent evaluation of the centers' operations will be conducted no later than 18 months after their opening to see whether the IMF will establish another three centers to cover all of sub-Saharan Africa. The Executive Board also approved the IMF's membership in the African Capacity Building Foundation (ACBF), the implementing agency for the Partnership for Capacity Building in Africa.

Source: The Role of Development Assistance, World Bank 2002.

The IFC capacity building efforts include technical assistance programs(Table A3.1). As of June 30, 2001, the cumulative contributions to IFC-managed technical assistance programs reached $582 million, compared with a cumulative total of $525 million at the end of FY00. 71 percent of this amount comes from donor countries, 19 percent from World Bank Group, and the rest 10 percent from donor institutions[7]. In July 2000, the IFC launched the SME Capacity Building Facility (CBF) to help meet the enormous need for creative new approaches to assisting small businesses in developing countries. Administered by the SME Department with an initial US$7.1 million allocation from IFC, it is a flexible new quick-response instrument that helps the Bank Group, its partners, and local institutions to do more to serve SMEs, especially by creating sustainable, effective capacity at the local level. The IFC administer various technical assistance programs supported by donor countries, including the World Bank Group. The Technical Assistance Trust Fund (TATF) program, for example, finances various feasibility and prefeasibility studies and projects to advice on privatization, policies to strengthen the business environment in developing countries, social impacts of investment projects, capacity-building programs, and

corporate governance practices. In FY 2001, for example, TATF funded a leasing sector study in Central Asia, and sponsored a study of Internet service provision for "smart schools" in Egypt. It also helped develop rural electrification projects in Uganda. The IFC also helped establish or scale up commercial microfinance institutions in Chad, the Kyrgyz Republic as well as providing insurance and pension advisory in Albania and Kazakhstan. Through FY01, the donor community provided cumulative contributions of $137 million to support TATF programs, which includes a budgeting allocation from IFC's own resources totaling $6.7 million to date. Since the inception of the program in 1988, donors have approved more than 1,000 technical assistance projects.

At the regional level, the African Development Bank (AfDB) is also active in the area of capacity building in its member countries. Recently, the AfDB has signed an agreement with the government of Canada that made available a fund of Can$ 2.5 million for an operative period of four (4) years. The agreement will enable the AfDB Group to access an additional contribution of Can$2.5 million from the Federal Government of Canada to finance more development projects consistent with the agreed strategic objectives, primarily relating to the promotion of economic growth in RMC. Specifically, these new resources will be used to pursue efforts to reduce poverty, promote regional integration and the development of the private sector, enhance good governance, and improve project management as well as assist in project identification missions and the policy-making process related to sustainable development.

The WTO also has concerted efforts in providing trade-related technical assistance including human and institutional capacity building to help least-developed countries alleviate their resource constraints. At their first Conference in Singapore in December 1996, WTO Ministers adopted the Comprehensive and Integrated *WTO Plan of Action for the Least-Developed Countries* which "envisaged a closer cooperation between WTO and other multilateral agencies assisting least-developed countries" in the area of trade. The plan is aimed at improving the overall capacity of least-developed countries to respond to the challenges and opportunities offered by the trading system.

Although many IDB member countries are full members of the WTO, and others are currently negotiating their membership, they still suffer from significant trade barriers. For example, some OECD countries still maintain significant barriers to trade from developing countries. Average tariffs range from 4.3 per cent (Japan) to 8.3 per cent (Canada). Products subject to high tariffs include major agricultural staple food products such as meat, sugar, and dairy products where tariffs sometimes exceeds 100 per cent; some fruits and vegetables (e.g., bananas) are hit with a 180 per cent tariff by the European Union; and textiles, clothing, and footwear, where tariff rates range between 15 and 30 per cent . These are example of products in which many member countries have a comparative advantage and where such protection can cause serious damages. The recent round of global trade negotiations, held in Doha, Qatar focused on agriculture and better access to agricultural markets (Box 5.6).

Box 5.6 The WTO "Doha Round" and IDB Member Countries

The recent round of global trade negotiations, dubbed the Doha Development Round, began in January 2002. The negotiations are focused on agriculture and so are crucial for mitigating the resource constraints faced by IDB member countries. The WTO member countries have agreed to negotiate better access to their agricultural markets, reduce trade-distorting support to domestic agriculture, and eventually eliminate subsidies for agricultural exports. Since the majority of IDB member countries depend on primary commodity exports, such measures, if undertaken, would certainly enable these countries to compete more effectively in export markets and could generate additional resources to mitigate their resource constraints.
The IDB member countries' main goal during the negotiations are for WTO members to:

- Substantially reduce or eliminate all tariffs on agricultural products
- Substantially reduce or eliminate tariff escalation
- Simplify complex tariffs
- Substantially reduce or eliminate market-distorting export subsidies and Domestic support
- Recognize the special needs of the world's least developing countries.

Adopted from ECA Annual Report 2002.

The WTO, UNCTAD and International Trade Center (ITC), in collaboration with the staff of the IMF, the World Bank and the UNDP, agreed that an Integrated Framework for the provision of trade-related technical assistance, including human and institutional capacity building, should be formulated. The Integrated Framework is meant to support trade and trade-related activities of the least-developed countries, including efforts to enhance the supply response of these countries. In particular, the program aimed at building institutions to handle trade policy issues, strengthening of export supply capabilities, strengthening trade support services, strengthening trade facilitation capabilities, training and human resource development, and assistance in the creation of supportive trade-related regulatory and policy framework that will encourage trade and investment. The technical assistance, which is normally provided to developing and least developing countries on a case-by-case basis, provide trade information and trade-related legal support, as well as improve their supply capabilities in order to make them more active players in the field of multilateral trade. Moreover, the six agencies will coordinate closely in applying the Integrated Framework for Trade-Related Technical assistance to least-developed countries.

5.5 Microfinance and Resource Constraints

Microfinance- the provision of small loans to the self-employed poor- gives the recipients a chance to start tiny businesses and build them into enduring sources of steady income. Expanding the poor's access to essential financial services has proven to be an effective poverty alleviation tool. There is a growing body of evidence drawn from the microfinance experience in many countries that not only are borrowers that were previously thought uncreditworthy able to pay for their micro credit but that there are significant non-financial benefits. Microfinance is expected to provide low-income people with a valuable service at an initial,

affordable cost to governments and donors. A widespread lending of capital on a micro basis throughout the developing world could promote growth at the community level, mitigate the resource constraints and eventually contribute to sustainable development in many poor countries. Generally, microfinance programs are characterized by: small, usually short-term loans, and secure savings product; streamlined, simplified borrower and investment appraisal; alternative approaches to collateral; quick disbursement of repeat loans after timely payment; above-market interest rates to cover the high transaction costs inherent in microfinance; high payment rates; and convenient location and timing of services (see, Dhumale and Sapcanin 2002).

The multilateral institutions hold out high hopes for microfinance as a vehicle for promoting economic growth and alleviating poverty. Specifically, microfinance is seen as a powerful tool for reaching the poor, raising their living standards, creating jobs, boosting demand for goods and services, contributing to economic growth and alleviating poverty. The World Bank has a global initiative to help the poor in the least developing countries using microfinance (see Box 5.7)[8]. The World Bank Group helps microfinance institutions scale up operations with long-term loans channeled through intermediaries and helps coordinate the global microfinance effort by hosting the Consultative Group to Assist the Poorest (CGAP), a consortium of 27 bilateral and multilateral donors that support microfinance (Box 5.6). IFC complements this work by providing private-sector know-how, technical training, and financing that helps existing institutions strengthen themselves and expand by becoming full-fledged commercial enterprises (World Bank: Review of SME Activities, 2001).

An increasing number of successful microfinance approaches are emerging worldwide now and there is a clear need to scale up the overall impact of microfinance, building on the models that are commercially viable. A recent World Bank survey found that there are more than 60 microfinance programs in the Middle East and North Africa (MENA) region, with an outstanding loan portfolio of nearly $100 million and more than 112,000 active borrowers[9]. Moreover, the World Bank survey found that only one commercial bank-Egypt's National Bank for Development-is active in the microfinance industry, indicating that the formal financial sector in the region has played minimum role in the spread of microfinance.

Box 5.7 CGAP: Providing Performance-Based Aid to Micro Lenders

Microfinance offers valuable lessons for improving the effectiveness of other areas of development assistance, especially those that address development of the private and financial sectors. The Consultative Group to Assist the Poorest, or CGAP—a Bank global initiative—was established in 1995 to help provide assistance to donors active in microfinance. It provides a vehicle for structured learning and dissemination of best practices on delivering financial and other services to the very poor on a sustainable basis. It also attempts to expand the resources reaching the economically active poor, and improves donor coordination for systematic financing of such programs. CGAP has provided performance-based grant support to 60 institutions in 47 countries, for a total of $27 million.

Using its grant fund, CGAP has developed an investment-style approach to grant-making that ties tranched funding to institutional needs and performance. The "dividends" or "outputs" to CGAP are the achievement of financial performance measures that will enable that microfinance institution to reach sustainability, and thus reach significant numbers of poor clients. The performance contract that accompanies CGAP's equity-like funding leaves the use of funds entirely at the discretion of management; reporting, monitoring, and continuation of disbursements are tied to the microfinance institution's fulfillment of performance thresholds at the institutional level. These thresholds are designed to lead the microfinance institution to full financial sustainability—that is, the ability to cover all costs including a commercial cost of funds. The thresholds generally step up over time and include indicators such as profitability, efficiency (cost per currency unit lent), portfolio quality, and growth (numbers of clients reached). Because most of a microfinance institution's funding is usually below market rates, achievement of full financial sustainability implies that it will generate substantial surpluses that will be retained to fund yet more services to poor clients. A successful CGAP client is Foundation Zakoura, the second largest microfinance institution in Morocco, which has over 35,000 active clients and has grown rapidly in recent.

Source: The Role and Effectiveness of Development Assistance, World Bank, Washington, DC, March 2002.

A good example of using microfinance to reduce poverty can be cited from Bangladesh and Indonesia. In Indonesia, sustainable microfinance in the formal sector began in 1970 with the opening of Bank Dagang Bali (BDB) and attained nationwide coverage with the 1984 structuring of the unit *desa*, or local banking, system of the state-owned Bank Rakyat Indonesia (BRI). BRI's unit desa system is now the largest financially self-sufficient provider of sustainable microfinance in the developing world. Microfinance has provided poor people in Indonesia with new opportunities for economic growth and financial security. Indonesia's approach to microfinance- making it profitable and widely available-helped the country reduce poverty from 40 percent of the population in the mid-1970s to about 11 percent in 1996 (Robison, 2001). The Grameen Bank experience in Bangladesh was another success story to cite in this context.

The African Development Fund (ADF) has recently undertaken the ADF Microfinance Initiative for Africa (AMINA). AMINA Program is intended as an innovative approach to increasing the capacity of existing microfinance institutions to deliver an appropriate range of financial services to microentrepreneurs. During its two-year pilot phase, the AMINA Unit will deliver an integrated program in support of microfinance institutions in selected African countries. These activities will include capacity building for partner microfinance institutions, including national and international NGOs, credit union federations, village banks and other formal institutions providing financial services to microentrepreneurs, especially women.

The AMINA program will deliver a range of services designed to enhance the partners ability to deliver these financial services on a sustainable basis. Support will include development of credit policies, operational procedures and management structures. Training activities, including credit analysis, portfolio management, delinquency control and the design and implementation of computerized Management Information Systems. AMINA will also identify an educational or training institution in each country selected for implementation during the pilot phase and seek to enhance its capacity to deliver training in microfinance-related issues.

5.6 Using Small and Medium Enterprises (SMEs) to Promote Growth

There is a general consensus among development economists and policymakers that private sector could be the engine of economic development in poor countries. In places plagued by exceedingly high levels of poverty and unemployment, "self employment" and micro-enterprise development is seen by many donor agencies as the only way to reach the "poorest of the poor." In particular, micro, small and medium enterprises are considered the lifeblood of developing economies, creating jobs and opportunities that are otherwise scarce. However, the mall and medium businesses in developing countries often lack the opportunities to sell their products in the global marketplace. The question to ask is, how can the SMEs sector in developing countries develop to assume competitive advantage and ensure active participation in the information economy that globalization engender? It is well known that entrepreneurs in poor countries lack access to formal financial markets and are instead limited to their own savings or less reliable sources of capital.

Because small business is a powerful force for poverty reduction, the World Bank Group has a substantial portfolio of SME-related investments. The Bank has high hopes on SMEs because they create jobs through which people can acquire skills and raise their incomes. Along with its partners, the Bank provides direct and indirect financing, training, technology, and support for improvements in business environment, better corporate governance and many other things that small businesses in developing countries need to grow. The World Bank lending for SMEs is currently found in a wide range of sectors. Most of its SME funding appears in the form of loans for agriculture, financial sector restructuring, private sector development, and other purposes. In the fiscal year running from June 30, 2000 to July 1, 2001, the World Bank Group had (Wortld Bank, WDR, 2001):

- Provided approximately $2.8 billion in SME support.
- Approximately 32 pilots and five new partnerships through the SME Capacity Building Facility, many of which complement or are part of new or existing IFC projects.
- Enhanced the impact of the IFC-managed SME Facilities by bringing them all under one organization and management structure and doing more to help them build a broader range of services, including development of local capacity.

- Assembled comprehensive pictures of the World Bank Group's regional programs for SME, and completed an initial set of SME "country maps".
- Distilled and disseminated examples of micro/SME "best practice" through a variety of new communications products (web page, newsletters, fact sheets, issues papers, etc.).
- Produced new metrics analyzing the outputs and impacts of the IFC/World Bank SME activities.

An example of the World Bank's support for SMEs in IDB member countries, is the $26 million Enterprise Development Project in Mozambique to help broaden the base of private participation in the economy. In addition to components that build technical capabilities of majority Mozambican-owned firms and help private and public institutions to deliver business support services, it provides two financial products available for firms in all sectors:

- A special facility designed to provide small, first-time bank borrowers with loans amounting to a maximum of $15,000.
- A traditional facility to finance loans up to $300,000 for small and medium-scale borrowers.

The financing facilities supported by this IDA credit provided medium-term loans for private borrowers' investments in the industrial, agro-processing, tourism, transportation, construction, and services sectors. The project is being carried out by a steering committee overseen by the Ministry of Industry, Trade and Tourism.

In 1996, the IFC launched a program called "Extending IFC's Reach" to promote private investment, including facilitation of private capital inflows in difficult market environment (IFC, Annual Report, 2001). The program places strong emphasis on the development of small and medium sized enterprises and technical assistance. The IFC provides a range of products and services to SMEs, including debt, equity, guarantees, and risk management (see Box 5.8). The Small and Medium Entreprise (SME) Department managed by IFC and the World Bank follows a four-part strategy to improve the business environment, build access to capital, provide support services, and advance information technology. Revising the trend where banks and other lenders view small business as a high-risk, the IFC and the World Bank are jointly assisting smaller businesses as well as local financial institutions in becoming more competitive. In FY01, they jointly launched a global initiative in e-finance, adapting proven lending techniques that revolutionized the U.S. market for small business credit in the 1990s. Better technology makes lending to small businesses more manageable and affordable to banks. IFC's investment in SMEs mainly comes through its financial market projects- i.e. creating, strengthening, and financing financial intermediaries that can efficiently channel capital to SME- with IFC also making amounts of direct investment in SMEs as well. IFC also offers significant support for SMEs through its project development facilities and Technical Assistance Trust Funds. The Multilateral Investment Guarantee Agency (MIGA) supports SMEs in the form of Guarantees.

Of the many SMEs activities coordinated by the IFC in IDB member countries, the following activities are noteworthy (IFC, Annual Report, 2001).

- *Cameroon*: The IFC conducted a $90 million to finance the privatization and restructuring of the state utility company (SONEL).
- *Mauritania*: The IFC conducted a $43 million financial restructuring for the privatization of national telecom operator (Mauritel).
- *Morocco*: IFC also helped attract $90 million from other lenders and raised $310 million from the international financial markets to structure the cellular phone company.
- *Egypt*: To support the generation of electric power, the IFC provided $90 million in loans.
- *Jordan*: The IFC provided $15 million to develop the Qualifying Industrial Zones (QIZs), special categories of export zones.
- *Tajikistan*: Through its capacity building programs, the IFC invested in an Audit and Consulting firm to provide a wide range of services on commercial basis to international and Tajik clients. Under this project, specialized field training in financial and business management will assist local entrepreneurs in operating businesses successfully in a market environment.

In Africa, SMEs account for the majority of private enterprises involving investment of less than US$ 5 million. Considering the importance of this sector in the African economies, an important objective of the African Development Bank (ADB) is to develop a dynamic small and medium enterprise (SME) sector in Africa. The ADB provides assistance to SMEs in the form of direct financial assistance, through lines of credit to financial institutions, and support facilities aimed at providing technical assistance to SMEs.

Box 5.8 Institute of SME Finance

To help ease the small business capital crunch, IFC recently took part in the creation of a new global nonprofit organization, the Institute for SME Finance (www.smeinstitute.org). Launched in Washington, DC in July 2000, the Institute promotes greater and more effective use of risk capital-based investment in growing entrepreneurial firms-especially those with no more than 100 employees and annual revenues of $5 million or less. Often the only kind of financing these companies can obtain is short-or medium-term debt secured by extensive collateral. In many cases a better alternative would be straight equity, debt/equity combinations, or long-term unsecured subordinated debt combined with a hands-on approach to investing.

The Institute, founded and managed by one of the world's leading experts in SME equity investment, Tom Gibson, is working on several fronts with investors, governments, development institutions, and others to help more SMEs obtain these appropriate forms of financing. Its key objectives include:

- Improving the SME sector's reputation among financial institutions
- Expanding access to long-term investment capital
- Improving enterprise performance through active investment strategies
- Promoting a local culture of equity investment
- Furthering linkages between the SME sector and local and international capital markets.

The Institute also received start-up funding from FUNDES International, The Multilateral Investment Fund, the Johns Hopkins University School for Advanced International Studies, and USAID.

Source: IFC Annual Report, 2001

In conclusion, it is safe to say that SMEs can be a true engine for growth in LDCs. Expanding the SME sector and providing the necessary finances can play a major role in mitigating the resource constraints faced by many poor countries, including the LDMCs. Since most of the population in LDMCs live and work in rural areas, a strategy to promoting SMEs can greatly enhance rural development and reduce poverty. There are many ways where the IDB can be instrumental in executing such a strategy. First, the IDB can enhance the efficiency, effectiveness, and sustainability of SMEs by supplying the much-needed support such as keeping a continuous on-the-ground presence, providing technical assistance, disseminating policies, strategies and "best practices" which have been proven to be successful in promoting SMEs. Second, the IDB can facilitate the access of entrepreneurs to local financing by supporting institutions that deliver or capable of delivering credit to the very poor on a financially sustainable basis. It can also create its own credit facilities in rural areas, or collaborate with Islamic Banks, credit bureaus, CSO, and NGOs. Third, since accessing the market is essential for SMEs in member countries, the IDB can help (finance) building the necessary infrastructure that enable these institutions distribute and sell their products. Such a strategy will make SMEs in member countries commercially viable businesses that can integrate in the international trading systems.

5.7 Information Technology (IT) and Resource Constraints

Can the Information technology (IT) of the latest twentieth century help mitigate the resource constraints? Lessons drawn from countries that have embraced technology reveal that IT contributes to the future prosperity of a nation, transforming businesses, enhancing productivity, and diffusing crucial information (Akapelwa, 2001). IT has a positive impact on the factors creating enabling environment for private sector development. In addition, the information technology can play an important role in the development of SMEs. Electronic business (E-business) has become a tool for global business interactions that have changed the way people do business. E-business and e-commerce now cover a wide range of commercial activities, including marketing, sales promotion, contracts and supply transactions. The use of e-business will enable SMEs to access sources of capital available in different locations as well as in development institutions. SMEs using the cyberspace will be informed of the capital opportunities provided by financial institutions, bilateral funds, and governments facilities set for SMEs. The Internet will also provide education, training, and access to new ideas for those SMEs starting business. The Internet and e-business will provide SMEs with exposure and the ability to market and distribute their product at relatively low cost.

In most developed countries, e-business is taking a large share of total business and more businesses are building their own web-sites to take advantage of the opportunities provided by the Internet. The global exposure will certainly impact their revenues and help them overcome many of the financial and physical constraints they face. In the IDB member countries, there are many success stories from Malaysia, Morocco, Tunisia, Egypt, Sudan, and UAE. However, there are major constraints inhabiting a fast adoption of e-business in IDB member countries. These include: limited awareness of the relevance of IT for doing

business, policy and legal framework, costs, shortage of skills and manpower, and the inadequacy of the IT infrastructure. To close the technological gap, IDB member countries need to upgrade their technologies.

In order for e-business to contribute to the growth of the private sector in IDB member countries, national governments, multinational institutions, including the IDB need to do the following:

- Conduct a serious campaign to create awareness and commitment to the use of IT in business.
- Establish legal and regulatory framework to ensure security
- Provide financial assistance to build the required infrastructure and solicit capital for financing projects related to IT infrastructure.
- Enhance capacity building efforts in IT area by training the manpower necessary to support IT development.
- National governments should remove telecommunication monopolies and barriers in order to permit cross-border use of e-business.

5.8 The Role of the UN and its Agencies (UNCTAD, ECA, UNDP) in mitigating resource constraints.

The Millennium Development Goals (MDGs) contained in the United Nations Millennium Declaration have generated great interest and attracted broad support from the international community. There are now unprecedented efforts to make progress toward the common goal of eradicating poverty and achieving sustainable development. The recent UN Financing for Development (FfD) Conference held in Monterrey, Mexico (March 2002) (see Box 1.1), the Doha round of multilateral trade negotiation January 2002), the G8 Summit at Kananaskisa, Canada (June 2002), and the World Summit on Sustainable Development in Johannesburg (August 2002), are all key milestones in this process. The case for action is compelling and challenging; a comprehensive approach to the mobilization of external and domestic resources for development. To this end, the commitment of the multilateral institutions is required to ensure that the needs and opportunities of different countries are taken into account. The accelerated progress toward meeting the MDGs will require action by developing countries and intensified support and partnership from the international community, including the UN and its agencies. The number of people living in poverty is increasing in various regions of the world, and the poorest countries are failing to catch up with developed and other developing countries.

Realizing this alarming situation, the UN and its specialized agencies are exerting continuous efforts to increase incomes, reduce poverty, and alleviate the suffering of the world's poor. Toward this end, the UN is working to ensure that commitments made by the international community to increase ODA be fulfilled and resources are deployed more effectively than in the past (see, Global Poverty Report, 2002). The UN and its program-oriented agencies are working to create awareness about the severity of the crisis inflecting LDCs. In view of this, the UN and its agencies have organized many international conferences on education,

health, population, trade, development, population, women, and the environment. Agencies such as United Nations Development Program (UNDP), International Labor Organization (ILO), United Nations Conference on Trade and Development (UNCTAD), World Food Program, and UNHCR work diligently to build capacity and provide technical assistance and relief to the refugees and the displaced in many developing countries.

UNCTAD promotes development in two ways. One is by supporting multilateral policy discussions designed to promote international economic cooperation for development. The other is through its technical cooperation programs, which assist developing countries in overcoming practical obstacles to sustainable development (UNCTAD, LDCs 2000 Report)..
These programs seek to:

- contribute to a better understanding of international economic problems and of their solutions;
- assist countries strengthen their negotiating capacities as regards international trade, finance and investment;
- help countries improve systems and procedures for trade expansion in such areas as trade efficiency, customs, maritime transport, and for financial management;
- contribute to national policy development, in particular the relationship between trade, technology, finance and investment; and
- promote cooperation among developing countries.

A recent review of UNCTAD's technical cooperation by the Trade and Development Board, based on a report by independent consultants, concluded that "UNCTAD should remain a relatively small agency in the area of technical cooperation, but one that can play a vital and unique role by filling selected and strategic technical cooperation niches in the development and management of the international trade and financial system. Funding for UNCTAD's technical cooperation comes from UNDP, individual donor countries, the European Commission, development financing institutions (particularly the World Bank and the Inter-American Development Bank) and foundations. Increasingly though, developing countries themselves are financing UNCTAD technical cooperation activities in their own countries.

UNCTAD is currently implementing about 300 projects for an annual delivery of some US$20 million or so. Whilst all regions of the world participate in the technical cooperation programs, particular attention is paid to the dramatic needs of Africa and of least developed, land-locked and island countries.

As a policy-oriented entity, the Economic Commission for Africa (ECA), a UN agency, is dedicated for helping African countries improve their economic and social conditions in order to actively participate in the world economy. Recognizing that the majority of the African poor live and work in the rural areas, the ECA is proposing a new pro-poor agenda based on the need for a structural transformation of the African economies (see, Proceedings of the Sixth Session of

the Conference of African Ministers of Finance, Vol1, 1997).. The agenda entails a renewed emphasis on modern agriculture as the basis for industrialization; improving the quality of human capital through investment in education, harnessing the benefits of the information technology, and tackling diseases that deepen poverty. To this end, the ECA has focused on reducing rural poverty in Africa through (ECA Annual Report, 1999-2002):

- Working closely with donors as well as African countries to strengthen private sector institutions-typically but not exclusively, informal sectors – especially micro- finance institutions, SMEs, and rural institutions.
- Strengthening capacity-building programs related to economic and corporate governance in Africa, focusing on priority areas of implementing sound macroeconomic strategies, strengthening public finance management and accountability, protecting the integrity of monetary and financial systems, and strengthening accounting and auditing systems.
- Collaborating with bilateral and multilateral donors to put in place policies and strategies that facilitate the access of the poor to productive resources.
- Reinforcing the need for developing mechanisms for promoting viable micro-financing systems as a source for funding small-scale grassroots enterprises
- Designing mechanisms for the active involvement of formal financial institutions in the provision of micro-financing services.
- In view of this, the ECA is working to build managerial and technical capacities by organizing training workshops and seminars to disseminate the "best practices" which have been proven to be successful in other countries.
- Producing technical publications, and providing advisory services to the African countries through four regional training centers.
- Coordinating with civil society organizations (CSO), interest groups, and NGOs for engaging the poor in planning and implementing the development process.
- Strengthening Africa's physical and policy structure to meet the challenges of globalization and liberalization through providing technical assistance on financial sector reforms.
- Monitoring the performance of the African economies by producing "Economic Report on Africa", an annual publication tracking economic development in Africa.
- Creating awareness of the severity of the economic and financial crisis facing Africa.

The UNDP is addressing many dimensions of human development, including the Millennium Development Goals (MDGs). UNDP advocates for nationally owned solutions to poverty and helps to ensure their effectiveness by sponsoring innovative pilot projects; connecting countries to global best practices and resources; and promoting the role of women in development. It brings governments, and civil society organizations together to coordinate their efforts, and organizes training and capacity building workshops. By so doing, the UNDP is aiming at drawing lessons learned concerning, for example, the strengths and weaknesses of initiatives launched both inside and outside government, identifying

future steps for UNDP and its partners and exploring possibilities of synergy with other on-going policy initiatives such as debt reduction and relief.

The experience of MFIs in financing development lends insightful remarks, useful lessons, and practical policies that worked in successful countries. Such lessons could support the IDB member countries in their efforts to mitigate resource constraints in financing their development. The concluding chapter summarizes the main salient features of these experiences.

Endnotes of Chapter 5

[1] By external resources here, we mean resources mobilized by bilateral and multilateral institutions, including private capital flows.

[2] Aid takes many forms, but can be classified into two broad categories: development aid (comprising project aid, program aid, and technical assistance) and emergency assistance intended to provide relief from the effects of natural disasters and other destructive events such as war, rather than stimulate growth and development, see Tsikata (1998).

[3] In March 14, 2002, President Bush announced that the United States will increase its core assistance to developing countries by 50% over the next 3 years, resulting in a $5 billion annual increase over current levels by FY 2002. This increase will go to a new Millennium Challenge Account (MCA) that funds initiatives to improve the economies and standards of living in countries that commit to good governance, invest in health and education for the poor, and sound economic policies that foster enterprise and entrepreneurship.

[4] It is widely recognized that aligning donor programs with PRSP is crucial to sustaining this approach. In part, the PRSP approach has been designed to overcome long-standing problems of poor coordination, weak country ownership of donor-financed programs, and the fragmentation of governmental programs and institutions caused by multiple, and often inconsistent, donor interventions.

[5] It should be emphasized here that, to ensure the effectiveness of technical assistance and capacity building, developing countries should be more involved in the whole process, from design to implementation and evaluation. This would create a sense of ownership of these programs among policy makers and stakeholders.

[6] IMF's programs of macroeconomic and structural adjustment aimed at generating growth and reducing poverty typically cover a wide range of policy issues, including, inter alia, the foreign trade regime, labor market policies, social safety nets, agricultural policies, and environmental concerns. Many of these subjects are in the domain of the UN and its specialized agencies. Collaboration between the IMF and the UN on these subjects has grown at both the institutional level and the country level.

[7] Includes African development Bank, European Bank for Reconstruction and Development, European Community, the Inter-American Development Bank, Asian Development Bank, and UNDP.

[8] Recognizing that microfinance was rapidly evolving beyond projects and programs into an actual industry capable of providing financial services to the hundreds of millions of the world's poor on a permanent and sustainable basis, the World Bank helped create CGAP to set standards and guidelines for the microfinance industry, and to act as a convener, disseminator and catalyst for best practices for donors, microfinance institutions and the industry as a whole.

[9] It is estimated that there are more than 4.5 million entrepreneurial poor in the region who lack access to microfinance and who could absorb an estimated $1.5 billion in loans.

VI. CONCLUSION

In summing, it is worth emphasizing again the severity of the resource constraints, major among them financial, which limited the ability of the IDB member countries in achieving growth rates compatible with poverty reduction. The main challenge faced IDB member countries during the 1990s was the mobilization of enough resources to sustain sufficient investment levels to generate poverty-reducing growth. In this study, an attempt is made to identify the main factors constraining resource mobilization in IDB member countries. The following are some of the salient feature of the study.

First, the average GDP growth rate for the IDB member countries during the 1990-2000 was low (3.0 percent) compared to other developing countries (3.5 per cent), including the low income countries. Yet, this rate overshadows impressive growth patterns in some IDB member countries, and more prominently LDMCs in Africa. For example, Mozambique and Uganda have made notable achievements by sustaining growth (6.6 and 5.3 per cent respectively) and making significant steps toward achieving many of the Millenium Development Goals (MDGs). In both countries, appropriate macroeconomic policies coupled with the required institutional reforms and the support of their development partners have contributed significantly to this performance. Indeed, such experiences could provide useful lessons for the other IDB member countries to improve on.

For example, Mozambique, a post conflict country, started with weak initial conditions, but was able to lay the foundation for a successful privatization program in relatively short period. Similarly, Uganda was able to set an example for other countries on how the HIPC debt relief can help alleviate the resource constraint problem. Uganda is now hailed as the first country where appropriate macroeconomic policies were instrumental in alleviating the resource constraints.

Second, the large foreign debt and high interest rates, combined with adverse terms of trade, compounded by intermittent capital flights, made debt service payments difficult for many IDB member countries, particularly the LDMCs. Nearly one third of the IDB member countries are classified as severely indebted. In 1999, the debt service absorbed nearly one fifth of the IDB member countries' export earnings. In this regard, the Ugandan experience with the HIPIC initiative provides a number of policy lessons for member countries with similar conditions. Capacity building in debt management is necessary if the debt problems are to be minimized, because a considerable part of the Ugandan debt problem was due to lack of technical capacity and the absence of debt coordination with institutions involved in debt management.

Third, during the 1990-2000, with few exceptions, gross domestic ratios were low for most of the IDB member countries, and negative in others. Consequently, the average resource gaps were of significant magnitude, ranging between 51 per cent of GDP (Lebanon) and 2.5 per cent of GDP (Kazakhstan). This implies that most IDB member countries did not generate enough resources for their developmental needs, and resorted to external finance to bridge these resource gaps. In this context, it is critically important for the IDB member countries

to keep their resource gap within manageable limits to be able to maintain a stable macroeconomic environment. Otherwise the debt burden and the consequent outflow of factor payments could create conditions unsustainable in the long run.

To this end, foreign capital remains important for many member countries, even though much of it came in the form of ODA rather than FDI or portfolio investment. This was not the case, however, for few IDB member countries who succeeded in attracting foreign inflows to finance their resource gaps during the 1990s. In fact, about 90 per cent of the capital inflows were accruing to only five member countries (Siddig and Diabi, 2001).

Fourth, a number of factors have been detrimental to the flow of foreign resources, including persistent current account deficits, lack of adequate international reserves, unfavorable terms of trade, and debt service difficulties. Owing to persistent current account deficits, averaging more than 10 per cent of GDP for some low and middle-income IDB member countries, the prospects for attracting foreign savings did not materialize. Meanwhile, low foreign reserves coupled with persistent current account deficits also led to the heavy reliance of many IDB member countries on foreign financing, especially bilateral and multilateral loans, to bridge their financing gaps. This, naturally, contributed to the build-up of a sizable external debt, which increased by 60 percent during 1990s to reach US$ 577 billion in 1999.

Fifth, the persistence of budget deficits in the majority of the IDB member countries during the 1990s (ranging between an annual average ratio of 0.4 and 17.4 per cent of GDP) deepened their resource constraints for financing development. More specifically, the crowding out effects of these fiscal deficits are more evident when public spending is predominantly in the form of unproductive government consumption. However, there is a scope for many of the IDB member countries to relax their fiscal constraints and enhance domestic resource mobilization. In particular, they can increase tax revenues through tax rationalization, or by broadening the tax base. Meanwhile, the privatization of state-owned enterprises generate additional resource to the budget. The continued dominance of the public sector in these economies has become a serious burden and imparted a high cost to economic development.

Sixth, financial sectors in most IDB member countries seem to lack the required depth and breadth needed for efficient operation. In addition, more than half of the IDB member countries does not have official stock markets and only very few member countries have a well-established capital market that has grown in scope and content. The number of listed companies are usually very small and negligible in some cases; traded shares are also very small; and market capitalization as a share of GDP ranged between 0.1 per cent (Azerbaijan) and 195 per cent (Malaysia). Consequently, consistent financial reforms remain a critical challenge for IDB member countries, particularly in the context of growing financial innovation and globalization.

Another striking feature of the IDB member countries financial sector is the absence of adequate rural finance. The fact that the majority of the poor in the IDB

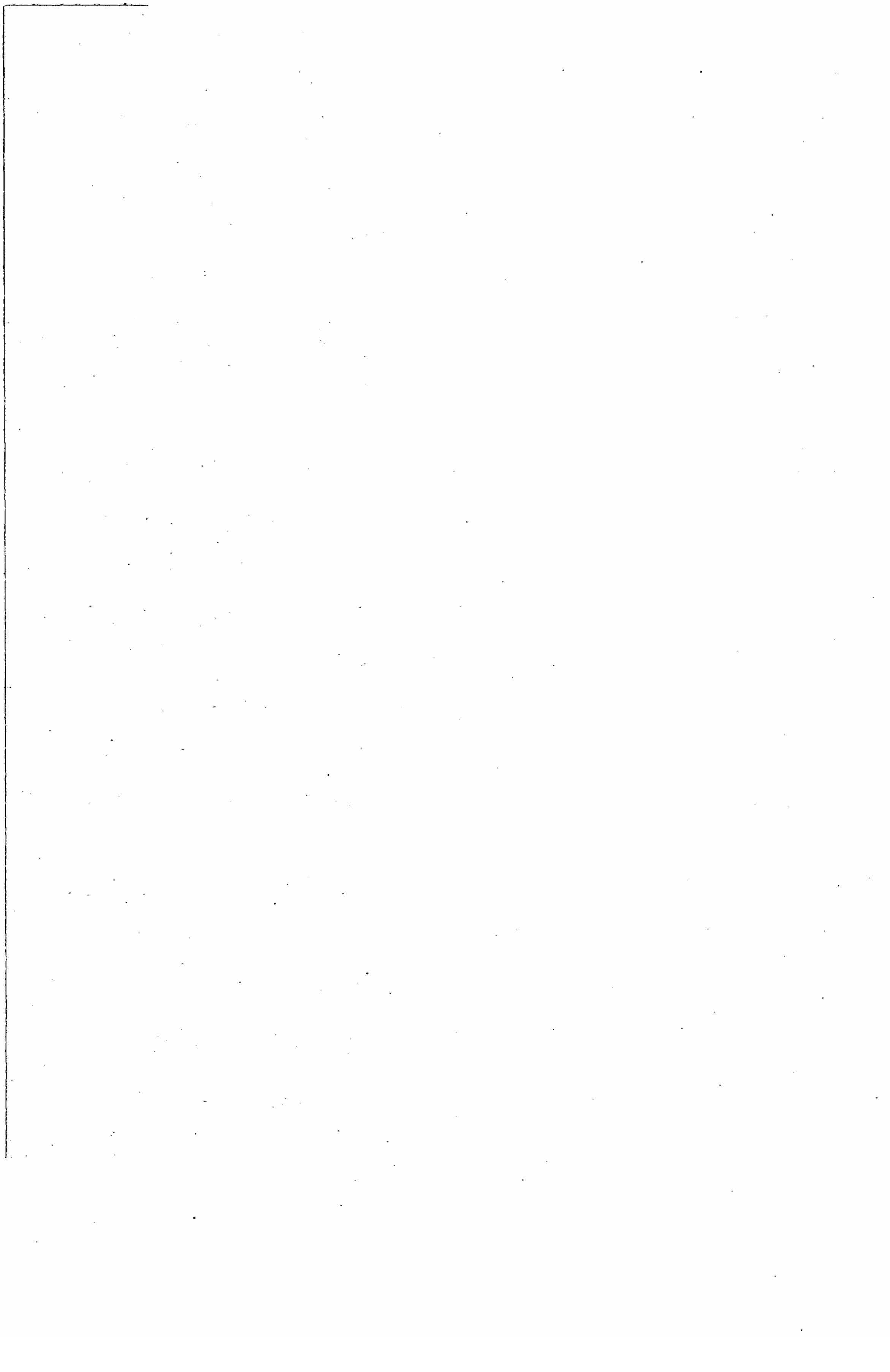
member countries lives and works in the rural areas entails the development of rural financial institutions to provide credit and promote saving. Conscious efforts have already been made to spread banking facilities to the rural sector in some IDB member countries (e.g., Bangladesh and Indonesia). Yet, the need for more rural finance to promote rural savings is overwhelming.

To this end, there are other factors than the macroeconomic, financial, and external conditions that have constrained resources for financing development in IDB member countries. Institutional constraints such weak institutions, poor legal systems, lack of consistency of reforms and bad governance have also exacerbated domestic resource constraints and contributed to the shun of private capital flows to many IDB member countries.

Seventh, the critical review of specific policies and programs-Islamic finance, microfinance, debt relief and SMEs-adopted in Sudan, Bangladesh and Uganda offered a number of useful lessons for the other IDB member countries. First, Islamic finance in Sudan is a learning- by- doing experience that could be improved on. The institutionalization of the Zakat and the securitization of Musharaka contracts have the potential of mobilizing savings, promoting rural development and reducing poverty. Second, despite all the criticisms, micro-finance programs as implemented in Bangladesh were able to engage the poor in the development process and mobilize their financial resources. The Grameen Bank's experience and its replicas proved that microfinance could be instrumental in relaxing resource constraints and reducing poverty. Moreover, the Grameen experience should be looked into from an Islamic perspective and replicated in IDB member countries. Third, the debt relief program in Uganda has released much needed resources that were used to fight poverty and enable the member country to work towards achieving many of the MDGs. Additionally, expanding the SME sector and providing the necessary finances can play a major role in mitigating the resource constraints faced by many LDMCs, particularly in rural areas.

Finally, there is an urgent need for strong partnership and collaboration with bilateral and multilateral donors to put in place policies and strategies that facilitate the access of the poor to productive resources. To this end, the major multinational financial institutions have played a major role in helping poor countries overcome their resource constraints and respond to the challenges of poverty reduction. The successful policy prescriptions include development aid, debt relief, microfinance, SMEs, and capacity building programs.

The role played by civil society organizations (CSO) and NGOs in engaging the people in their own development should be acknowledged as well. Indeed, these organizations have a comparative advantage in mobilizing resources from external sources and directly putting them in various investment opportunities, and facilitate their engagement with the private sector through institutions building (SMEs, micro-finance). In addition, their calls for improved governance, transparency, accountability, and the rule of law can help governments make informed decisions.



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ANNEX

Table A1.1 GDP growth in IDB Member Countries (annual %) 1990-2000

	GDP growth (annual %)												Mean		SD
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	90-00	95-00	90-00	
Albania	-9.6	-27.5	-7.2	9.6	9.4	8.9	9.1	-7.0	7.9	7.3	7.8	-2.7	5.7	0.8	12.1
Algeria	0.8	-1.2	1.8	-2.1	-0.9	3.8	4.1	1.1	5.1	3.2	2.4	0.4	3.3	1.6	2.4
Azerbaijan	-11.7	-0.7	-35.2	-11.8	-19.7	-11.8	1.3	5.8	10.0	7.4	11.1	-15.2	4.0	-5.0	14.4
Bahrain	4.4	11.2	6.7	12.9	-0.3	3.9	4.1	3.1	4.8	4.0	..	6.5	4.0	5.5	3.9
Bangladesh	6.6	3.3	5.0	4.6	4.1	4.9	4.6	5.4	5.2	4.9	5.9	4.8	5.2	5.0	0.9
Benin	3.2	4.7	4.0	3.5	4.4	4.6	5.5	5.7	4.6	4.7	5.8	4.1	5.2	4.6	0.8
Brunei	2.7	4.0	-1.1	0.5	1.8	3.1	3.6	4.1	1.0	..	..	1.8	2.9	2.2	1.8
Burkina Faso	-1.5	10.0	2.5	4.9	1.4	4.5	7.5	4.8	6.4	6.3	2.2	3.6	5.3	4.4	3.2
Cameroon	-6.1	-3.8	-3.1	-3.2	-2.5	3.3	5.0	5.1	5.0	4.4	4.2	-2.6	4.5	0.8	4.4
Chad	-4.2	8.5	8.0	-15.7	10.1	0.8	2.4	4.3	7.3	1.0	0.6	1.3	2.7	2.1	7.3
Comoros	5.1	-5.4	8.5	3.0	-5.3	-3.9	-1.3	4.2	1.2	1.9	-1.1	0.3	0.2	0.6	4.5
Djibouti	-1.9	0.5	-0.2	-3.9	-2.9	-2.3	-3.3	-0.6	0.5	2.2	0.7	-1.8	-0.5	-1.0	2.0
Egypt	5.7	1.1	4.4	2.9	3.9	4.7	5.0	5.5	5.6	6.0	5.1	3.8	5.3	4.5	1.5
Gabon	5.2	6.1	-3.3	2.4	3.4	7.0	5.2	5.8	2.1	-6.2	2.0	3.5	2.6	2.7	4.1
Gambia	3.6	3.1	3.4	3.0	0.2	0.9	2.2	4.9	4.9	6.4	5.6	2.3	4.2	3.5	1.9
Guinea	4.4	0.8	2.9	4.2	6.3	4.4	4.6	4.8	4.6	3.6	2.0	3.8	4.0	3.9	1.5
Guinea-Bissau	6.1	5.1	1.1	2.1	3.2	4.4	11.6	6.5	-28.1	7.8	7.5	3.7	1.6	2.5	10.6
Indonesia	9.0	8.9	7.2	7.3	7.5	8.4	7.6	4.7	-13.1	0.8	4.8	8.1	2.2	4.8	6.4
Iran	11.2	10.6	6.1	2.1	0.9	2.9	5.5	3.4	2.0	2.5	5.4	5.6	3.6	4.8	3.5
Jordan	1.0	1.8	18.8	4.6	5.0	6.4	2.1	3.1	2.9	3.1	3.9	6.3	3.6	4.8	4.9
Kazakhstan	-4.6	-11.0	-5.3	-9.2	-12.6	-8.2	0.5	1.7	-1.9	2.7	9.6	-8.5	0.7	-3.5	6.7
Kuwait	..	..	..	34.0	8.4	1.1	-3.3	1.0	3.7	-1.7	1.7	14.5	0.4	5.6	12.0
Kyrgyz	5.7	-7.9	-13.9	-15.5	-20.1	-5.4	7.1	9.9	2.1	3.7	5.0	-9.5	3.7	-2.7	10.4
Lebanon	26.5	38.2	4.5	7.0	8.0	6.5	4.0	4.0	3.0	1.0	0.0	15.1	3.1	9.3	11.9
Malaysia	9.0	9.5	8.9	9.9	9.2	9.8	10.0	7.3	-7.4	6.1	8.3	9.4	5.7	7.3	5.0
Maldives	17.0	1.4	6.7	5.6	7.7	13.0	9.1	10.2	8.2	7.4	4.8	8.6	8.8	8.3	4.1
Mali	-1.9	1.6	8.3	-2.1	0.9	6.2	3.2	6.8	3.4	6.1	4.5	2.2	5.1	3.4	3.5
Mauritania	-1.8	2.6	1.7	5.5	4.6	4.6	5.5	3.2	3.7	4.1	5.2	2.9	4.4	3.5	2.1
Morocco	4.0	6.9	-4.0	-1.0	10.4	-6.6	12.2	-2.2	7.7	0.0	0.9	1.6	2.0	2.6	6.1
Mozambique	1.0	4.9	-8.1	8.7	7.5	4.3	7.1	11.0	12.6	7.5	1.6	3.0	7.4	5.3	5.7
Niger	-1.3	2.5	-6.5	1.4	4.0	2.6	3.4	2.8	10.4	-0.6	0.1	0.5	3.1	1.7	4.1
Oman	7.5	9.2	6.8	7.0	3.5	3.2	..	..	..	..	..	6.2	3.2	6.2	2.4
Pakistan	4.5	5.5	7.8	1.9	3.9	5.1	3.9	1.0	2.6	3.7	4.4	4.8	3.4	4.0	1.8
Saudi Arabia	8.6	10.5	2.8	-0.6	0.5	0.4	1.4	2.0	1.7	-0.8	4.5	3.7	1.5	2.8	3.7
Senegal	3.9	-0.4	2.2	-2.2	2.9	5.2	5.1	5.2	5.7	5.1	5.6	1.9	5.3	3.5	2.7
Sierra Leone	4.8	-8.0	-9.6	0.1	6.7	-10.6	1.7	-17.0	2.8	-11.3	7.0	-2.8	-4.6	-3.0	8.4
Sudan	-0.4	6.0	4.9	4.3	4.0	25.2	4.0	9.7	6.1	5.2	8.3	7.3	9.7	7.0	6.5
Suriname	0.1	2.9	4.3	-3.0	-2.3	2.3	21.0	5.0	4.7	-3.7	-7.3	0.7	3.7	2.2	7.4
Syria	7.6	7.9	13.5	5.2	7.7	5.8	7.3	2.5	7.6	-1.8	2.5	7.9	4.0	6.0	3.9
Tajikistan	-0.6	-7.1	-29.0	-16.4	-21.3	-12.4	-16.7	1.7	5.3	3.7	8.3	-14.5	-1.7	-7.7	12.3
Togo	-0.2	-0.7	-4.0	-15.1	15.0	7.8	8.8	4.3	-2.1	2.4	-0.7	0.5	3.4	1.4	7.8
Tunisia	8.0	3.9	7.8	2.2	3.3	2.3	7.1	5.4	4.8	6.1	4.7	4.6	5.1	5.0	2.0
Turkey	9.3	1.0	5.8	8.3	-5.8	7.3	6.8	7.5	3.1	-5.1	7.2	4.3	4.5	4.1	5.3
Turkmenistan	0.7	-4.7	-5.3	-10.0	-17.3	-7.2	-6.7	-11.3	7.0	17.0	17.6	-7.3	2.7	-1.8	11.3
Uganda	6.5	5.6	3.4	8.3	6.4	11.5	9.1	4.7	5.6	7.5	3.5	6.9	7.0	6.6	2.4
UAE	17.5	0.2	2.7	-0.9	2.2	6.1	10.0	2.1	-5.7	..	..	4.6	3.2	3.8	6.7
Yemen	..	2.0	8.3	4.1	2.2	10.9	5.9	8.1	4.9	3.7	5.1	5.5	6.4	5.5	2.8

Source: WDI, World bank, 2001

Table A1.2 GDP per capita growth in IDB Member Countries (annual %) 1990-2000

	GDP per capita growth (annual %)											Mean			SD
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	90-00	95-00	90-00	
Albania	-10.7	-26.3	-5.9	9.4	8.0	7.5	7.8	-8.0	7.1	6.6	6.9	-3.0	4.7	0.2	11.5
Algeria	-1.8	-3.6	-0.6	-4.4	-3.1	1.7	2.3	-0.6	3.5	1.7	0.9	-2.0	1.6	-0.4	2.6
Azerbaijan	-12.6	-2.2	-36.2	-13.2	-20.8	-12.8	0.3	4.8	9.0	6.5	10.2	-16.3	3.0	-6.1	14.4
Bahrain	1.5	10.1	4.4	9.1	-3.8	0.3	0.3	-0.4	1.0	0.3	..	3.6	0.3	2.3	4.4
Bangladesh	4.1	1.5	3.2	2.8	2.3	3.1	2.8	3.6	3.4	3.1	4.1	2.8	3.3	3.1	0.8
Benin	0.0	1.5	0.5	0.4	1.3	1.8	2.7	2.9	1.9	2.0	3.1	0.9	2.4	1.6	1.0
Brunei	-0.3	1.0	-4.0	-2.4	-1.1	0.2	0.8	1.3	-1.6	..	..	-1.1	0.2	-0.7	1.8
Burkina Faso	-3.8	7.4	0.1	2.4	-1.0	2.1	5.0	2.3	3.9	3.7	-0.4	1.2	2.8	2.0	3.1
Cameroon	-8.9	-6.5	-5.8	-5.8	-5.0	0.8	2.5	2.7	2.7	2.1	2.0	-5.2	2.1	-1.7	11.5
Chad	-6.3	5.9	5.0	-18.3	6.5	-2.8	-0.4	1.5	4.4	-1.8	-2.1	-1.7	-0.2	-0.8	2.6
Comoros	2.4	-7.8	5.7	0.4	-7.7	-6.3	-3.8	1.6	-1.3	-0.6	-3.6	-2.2	-2.3	-1.9	14.4
Djibouti	-10.0	-6.4	-5.7	-7.9	-5.5	-3.5	-4.7	-2.2	-1.2	0.3	-1.3	-6.5	-2.1	-4.4	4.4
Egypt	3.3	-1.1	2.2	0.8	1.9	2.7	3.1	3.5	3.6	4.0	3.1	1.6	3.3	2.5	0.8
Gabon	2.0	3.0	-6.0	-0.5	0.6	4.1	2.4	3.0	-0.6	-8.6	-0.6	0.5	-0.1	-0.1	1.0
Gambia	-1.1	-1.2	-0.6	-0.7	-3.2	-2.2	-0.9	1.7	1.7	3.1	2.3	-1.5	1.0	-0.1	1.8
Guinea	1.4	-2.0	0.0	1.5	3.6	1.8	2.0	2.3	2.2	1.3	-0.3	1.0	1.6	1.2	3.1
Guinea-Bissau	4.2	1.9	-1.6	-0.4	0.8	2.0	9.1	4.3	-29.6	5.6	5.2	1.1	-0.6	0.1	4.6
Indonesia	7.1	7.0	5.4	5.5	5.8	6.6	5.9	3.0	-14.5	-0.8	3.1	6.2	0.6	3.1	7.1
Iran.	8.8	8.9	4.4	0.5	-0.7	1.2	3.9	1.7	0.4	1.0	3.9	3.9	2.0	3.1	4.4
Jordan	-2.7	-8.9	12.8	0.0	1.0	3.0	-1.0	0.0	-0.2	0.0	0.8	0.9	0.4	0.4	3.1
Kazakhstan	-4.7	-10.8	-5.0	-8.7	-11.8	-7.3	1.8	3.3	-0.2	3.7	10.0	-8.0	1.9	-2.7	1.5
Kuwait	..	..	..	30.4	5.4	-4.1	-9.7	-5.3	0.5	-4.7	-1.4	10.6	-4.1	1.4	4.0
Kyrgyz	4.1	-9.1	-14.7	-15.3	-19.9	-6.3	5.6	7.4	-0.3	2.2	3.9	-10.2	2.1	-3.8	2.0
Lebanon	-24.1	35.5	2.5	4.9	6.0	4.5	2.2	2.3	1.4	-0.4	-1.3	12.9	1.4	7.4	1.5
Malaysia	5.8	6.9	6.2	7.2	6.5	7.1	7.3	4.7	-9.5	3.6	5.7	6.6	3.1	4.7	10.3
Maldives	13.7	-1.2	3.9	2.8	4.9	10.1	6.3	7.3	5.4	4.7	2.3	5.7	6.0	5.5	6.3
Mali	-4.6	-1.1	5.5	-4.6	-1.6	3.7	0.8	4.2	1.0	3.6	2.1	-0.5	2.6	0.8	3.3
Mauritania	-4.1	0.1	-0.9	2.7	1.8	1.7	2.5	0.1	0.5	0.7	1.7	0.2	1.2	0.6	5.1
Morocco	1.9	4.8	-5.9	-2.8	8.4	-8.2	10.3	-3.9	5.9	-1.6	-0.8	-0.3	0.3	0.7	6.9
Mozambique	0.2	2.9	-9.8	6.4	4.6	1.7	4.4	8.4	10.4	5.4	-0.7			3.1	12.5
Niger	-4.4	-0.6	-9.5	-2.0	0.5	-0.9	-0.1	-0.8	6.6	-3.9	-3.2	-2.8	-0.4	-1.7	9.6
Oman	4.2	0.8	-0.6	0.3	0.6	0.3	..	..	..	..	..	1.0	0.3	1.0	11.6
Pakistan	1.8	2.8	5.2	-0.6	1.3	2.6	1.3	-1.4	0.1	1.2	1.9	2.2	1.0	1.5	4.8
Saudi Arabia	3.9	7.1	-0.4	-3.2	-2.1	-2.2	-1.2	-0.6	-0.9	-3.3	1.8	0.5	-1.1	-0.1	4.0
Senegal	1.1	-2.4	-0.2	-4.7	0.2	2.4	2.2	2.2	2.7	2.3	2.9	-0.6	2.5	0.8	3.5
Sierra Leone	2.5	-10.1	-11.8	-2.3	4.2	-12.8	-0.7	-18.9	0.6	-13.1	4.9			-5.2	1.9
Sudan	-2.3	3.9	2.6	1.9	1.4	21.8	1.4	7.2	3.9	3.2	6.4	4.9	7.3	4.7	6.0
Suriname	-0.6	2.4	4.0	-3.3	-2.6	2.0	20.6	4.7	4.4	-4.1	-7.9	0.3	3.3	1.8	5.4
Syria	4.1	4.4	9.8	1.9	4.3	2.5	4.4	-0.2	4.9	-4.2	0.0	4.5	1.2	2.9	3.9
Tajikistan	-2.9	-9.8	-30.4	-17.4	-22.8	-13.8	-18.0	0.2	3.4	3.2	8.1	-16.2	-2.8	-9.1	1.6
Togo	-2.4	-3.0	-6.3	-17.2	12.1	5.0	5.9	1.3	-4.9	-0.7	-3.7	-2.0	0.5	-1.3	1.8
Tunisia	5.4	1.9	5.6	0.2	1.4	0.7	5.5	4.0	3.4	4.7	3.5			3.3	3.2
Turkey	6.9	-0.6	4.2	6.7	-7.2	5.7	5.2	5.9	1.6	-6.5	5.6	2.6	2.9	2.5	2.4
Turkmenistan	-1.7	-9.3	-10.4	-13.5	-20.4	-9.9	-9.0	-13.7	3.9	12.9	15.3	-10.9	-0.1	-5.1	8.3
Uganda	2.8	2.0	0.0	4.9	3.1	8.1	5.8	1.6	2.5	4.6	0.8	3.5	3.9	3.3	6.2
UAE	8.7	-8.1	-0.9	-7.4	-0.3	3.6	4.8	-2.7	-10.6	..	..	-0.7	-1.2	-1.4	7.4
Yemen	..	-9.7	4.9	0.7	-1.1	7.5	2.9	5.1	2.0	1.0	2.4	0.5	3.5	1.6	3.6

Source: WDI, World bank, 2001

Table A 2.1: Aggregate net resource Flows (Millions US$)

											90-95			95-99			90-99		
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Mean	SD	CV	Mean	SD	CV	Mean	SD	CV
All developing countries	98529	1E+05	2E+05	219169	220356	257172	313143	343726	318325	290699	178627	62739	0.35	304613	32538	0.11	233765	86092	0.37
East Asia & Pacific	27026	35308	53705	82353	90398	108095	126254	127685	82838	89216	66148	32393	0.49	106818	20614	0.19	82288	34724	0.42
Europe & Central Asia	12591	17171	27997	32281	22710	36914	48454	59849	59562	45063	24944	9213	0.37	49968	9829	0.20	36259	16728	0.46
Middle East & North Africa	9910	12244	9028	9173	9778	3171	7401	8385	11472	19884	8884	3029	0.34	10063	6242	0.62	10045	4250	0.42
Other developing countries	35070	49617	61810	101149	105786	125199	126741	144496	127182	115471	79772	35854	0.45	127818	10476	0.08	99252	37343	0.38
South Asia	9221	10705	10389	12235	15253	9798	13878	13229	12586	11817	11267	2203	0.20	12262	1575	0.13	11911	1910	0.16
Sub-Saharan Africa	18082	17293	17227	17437	20528	23777	17696	21216	14895	17509	19057	2626	0.14	19019	3482	0.18	18566	2545	0.14
IDB	27681	31942	37281	38682	38360	39005	51359	50178	27190		35492	4638	0.13	41933	11295	0.27	37964	8580	0.23

Source: WDI, World Bank, 2001

Table A2.2 Official net resource flows (Millions US$)

											90-95			95-99			90-99		
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Mean	SD	CV	Mean	SD	CV	Mean	SD	CV
All developing countries	55922	62343	54011	53363	45912	53904	31003	39833	50624	51961	54243	5268	0.10	45465	9758	0.21	49888	8914	0.18
East Asia & Pacific	8306	8490	8927	10086	7771	11782	5578	18241	15589	15269	9227	1474	0.16	13292	4885	0.37	11004	4094	0.37
Europe & Central Asia	4942	13049	10854	11693	11813	10706	11244	9216	6220	6939	10510	2853	0.27	8865	2229	0.25	9668	2728	0.28
Middle East & North Africa	9542	9095	7076	5521	3358	1531	2273	-456	2249	3240	6021	3177	0.53	1767	1383	0.78	4343	3338	0.77
Other developing countries	14691	16750	18332	20530	15184	29305	5301	10238	15544	5741	19132	5423	0.28	13226	9895	0.75	15162	7087	0.47
South Asia	7046	8772	7100	5810	6078	3005	4845	3600	5005	6938	6302	1921	0.30	4679	1517	0.32	5820	1752	0.30
Sub-Saharan Africa	16798	15291	16238	14684	15619	14276	12149	11607	11444	10264	15484	943	0.06	11948	1472	0.12	13837	2286	0.17
IDB	21339	23046	17794	1436	13689	9151	6328	4879	10778		16565	5184	0.31	7784	2670	0.34	13486	6363	0.47

Source: WDI, World Bank, 2001

Table A2.3 Official development assistance and official aid (current millions US$)

											90-95			95-99			90-99	
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Mean	SD	CV	Mean	SD	CV	Mean	SD	CV
East Asia & Pacific	7826	7461	9863	9243	9431	9981	7791	6692	8225	9811	8968	1067	0.12	8500	1393	0.16	8632	1174	0.14
Europe & Central Asia	3567	8790	8251	9592	9728	11535	8647	6873	8434	10878	8577	2697	0.31	9273	1907	0.21	8630	2225	0.26
Middle East & North Africa	10347	10422	7138	5736	7194	5591	6032	5537	5313	5128	7738	2158	0.28	5520	341	0.06	6844	1993	0.29
South Asia	5985	7939	6629	5176	7057	5160	5164	4296	5025	4254	6324	1098	0.17	4780	464	0.10	5669	1209	0.21
Sub-Saharan Africa	18045	18026	19445	17499	19381	18846	16517	14945	14196	12546	18540	802	0.04	15410	2394	0.16	16945	2347	0.14
IDB	24055	24247	20623	18002	19454	16302	15137	13488	14489	13989	20447	3214	0.16	14681	1093	0.07	17979	4007	0.22
World	59710	67901	67184	62489	67506	68025	61983	53899	57252	59125	65469	3510	0.05	60057	5335	0.09	62507	5029	0.08

Source: WDI, World Bank, 2001

Table A2.4 Private net resource flows (Millions US$)

											90-95			95-99			90-99	
	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	Mean	SD	CV	Mean	SD	CV	Mean	SD	CV
All developing countries	42606	60870	99311	165806	174444	203268	282140	303894	267700	238738	124384	66022	0.53	259148	39189	0.15	183878	92572	0.50
East Asia & Pacific	18720	26819	44778	72267	82627	96313	120676	109444	67249	73947	56921	31499	0.55	93526	22760	0.24	71284	33529	0.47
Europe & Central Asia	7649	4122	17143	20587	10897	26208	37210	50633	53342	38124	14434	8351	0.58	41103	11028	0.27	26592	17559	0.66
Middle East & North Africa	369	3149	1952	3652	6420	1640	5127	8841	9223	16644	2864	2093	0.73	8295	5594	0.67	5702	4860	0.85
Other developing countries	20379	32867	43478	80619	90601	95894	121441	134257	111638	109730	60640	32331	0.53	114592	14279	0.12	84090	39235	0.47
South Asia	2174	1934	3289	6425	9176	6793	9033	9629	7580	4879	4965	2932	0.59	7583	1886	0.25	6091	2895	0.48
Sub-Saharan Africa	1283	2001	990	2752	4909	9501	5548	9609	3452	7245	3573	3225	0.90	7071	2636	0.37	4729	3205	0.68
IDB	6328	8905	19442	24079	24618	29838	40473	37431	17225	7927	18868	9353	0.50	26579	13755	0.52	21627	11996	0.55

Source: WDI, World Bank, 2001

Table A3.1: Resource mobilization from the primary and secondary Arab markets (Number* : million; Amount: million of US$)

Country		2000:IV		2001:I		2001:II		2001:III		2001:IV		Average
		Number	Amount	Number	Amount	Number	Amount	Number	Amount	Number	Amount	Amount
Jordan	Primary	3	44.1	3	69.53	5	3.1	2	3.9	2	0.11	24.1
	Secondary	35.6	78.56	47.09	89.21	69.31	180.6	118.6	370.1	100.11	294.5	202.6
		Market Cap	4943		5104		5249		5698		63148	16828
Bahrain	Primary	0	0	0	0	0	0	0	0	0	0	0.0
	Secondary	203.25	78.61	30.97	21.35	98.37	60.63	59.55	112.51	124.21	55.88	65.8
		Market Cap	6624		6247		6372		6384		6601	6446
Tunisia	Primary	0	0	1	5.13	1	2.39	1	4.54	1	1.7	2.8
	Secondary	6.36	139.23	5.96	106.35	6.43	96.92	3.62	55.64	5.28	83.14	96.3
		Market Cap	2809		2531		2305		2325		2230	2440
Saudi Arabia	Primary	0	0	0	0	0	0	0	0	0	0	0.0
	Secondary	129.42	3975.45	111.19	3928	250	7191.5	234	7352	95	3753	5240.0
		Market Cap	67166		67958		73485		69321		73201	70226
Oman	Primary	0	0	0	0	0	0	0	0	0	0	0.0
	Secondary	29.25	100.83	34.7	145.7	25.74	79.7	30.07	75.5	33.03	119	104.1
		Market Cap	3518		3132		3040		3202		2634.4	3105
Kuwait	Primary	0	0	0	0	0	0	0	0	0	0	0.0
	Secondary	861.06	654.74	2606.5	1962.26	4929.58	3027.45	5876.2	4704.62	7413.04	2016.83	2473.2
		Market Cap	19.848		22145.5		25699		26682		26662	20242
Lebanon	Primary	0	0	0	0	0	0	0	0	0	0	0.0
	Secondary	9.98	64.44	2.52	11.12	4.2	17.68	2.56	8.01	5.44	16.16	23.5
		Market Cap	1583		1335		1353		1120		1248	1328
Egypt	Primary	357	712.4	336	699	572	1103.4	422	1068.1	337	706.2	857.8
	Secondary	253	1895	316	1233	241	1488	317.3	1418	310.2	1775	1561.8
	Market Cap		30791		28604		28792		26528		24309	27805
Morocco	Primary	0	0	0	0	0	0	0	0	0	0	0.0
	Secondary	3.26	245	3.7	183.4	4.05	190	2.64	195.2	5.44	272.5	217.2
		Market Cap	10876		10948		9264		9165.4		9031	9857
All Arab Markets	Primary		757	340	774	578	1109	425	1077	340	708	885
	Secondary		7232	3159	7680	5629	12332	6645	14292	8092	8386	9984
		Market Cap	128330		148005		155559		150425		209064	158277

Table A4.1.1: The savings & Social development bank Finance by sector (1986-2000)

(Million Dinars)

	1986		1997		1998		1999		2000	
	Value	%	Value	%	Value	%	Value	%	Value	%
Agriculture	179	33.1	171	30.1	334.3	29.4				
Industry	72	14.2	51	9.0	95.8	8.4	472	20.0	769.3	32
Transport & storage	44	8.2	50	8.8	128.1	11.2				
Handicrafts	68	12.6	46	8.1	41.7	3.7	102.9	4.4	79.7	3.3
Household & small producers							223.4	9.4	228.6	9.5
Services	89	16.5	71	12.5	103.2	9				
Exports	35	6.5	57	10.0	71.3	6.2	111.2	4.7	94.2	3.9
Local trade	6	1.1	41	7.2	64.2	5.6	571	24.2	400	16.7
Direct investment	1	0.2	2	0.4	1.8	0.2	116	4.9	166	6.9
Staff loans	28	5.2	11	2.0	30.5	2.7	64	2.7	166	6.9
Social development	9	1.7	19	3.3	-	-	-	-	-	-
Finance	-	-	41	7.2	256.8	31.4	151	6.4	209	8.7
Others							44.5	1.9	54	2.2
	4	0.7	8	1.4	13.8	1.2				
							25.6	1.1	237	9.9
Total	540	100	068	100	1141.5	100	2357.9	100	2464	100

Source: Bank of Sudan Annual reports

Table A4.2.1: Comparative analysis of two groups of NGOs

Issues	Islamic NGOs	Secular NGOs
Target group of NGOs	Generally rural poor are the target population. Members can own maximum of 0.5 acres of land. Islami Bank also includes marginal farmers having maximum of 1.5 acres of land.	Generally rural poor are the target population. Members can own maximum of 0.5 acres of land.
Criteria applied for selection of members	Land ownership criteria	Land ownership criteria
Area of Operation	Rural area	Rural area
Gender	Both men and women are included in the groups. One NGO within the sample work only for men. Clear bias is to accept men but Islami Bank prefers women.	Normally, women are preferred in the by NGOs to form groups, although a small percent (5-10%) of members are men. One NGO within the present sample of NGOs work only for women.
Programs	Mainly micro-investment	• Mainly microcredit • Non-formal Education • Water and sanitation
Group size	5 to 30 members per group/society	5 to 30 members per group/society
Frequency of meeting	weekly/monthly	weekly/monthly
Terms and conditions of savings		
Savings of members	Taka 5-10 per week	Taka 5-10 per week
Interest/profit paid on savings	Variable: 5-6% per annum	5-6% per annum
Other savings instruments	None	None
Withdrawal of savings by members	Members are allowed to withdraw certain percent of savings.	Members are allowed to withdraw certain percent of savings.

Table A4.2.1: Comparative analysis of two groups of NGOs (Cont.)

Terms and conditions for loan		
Amount of loan Maximum Minimum	 Taka 3000 Taka 15,000 (Islami Bank)	 Taka 3000 Taka 10,000
Duration of loan	One year	One year
rate of interest/mark-up	12-15.5% mark-up (24-25%) rate of interest	30% per annum
Mode of repayment	Weekly installments	Weekly installments
Type of loan	Islamic mode of investment is used - mainly bye muazzal (sale on credit.)	Loan is provided in cash.
Activities financed	Common activities available in rural areas especially petty trading, rearing poultry and live stock, agricultural input, shop-keeping, rural vehicles	Common activities available in rural areas especially petty trading, rearing poultry and live stock, agricultural input, shop-keeping, rural vehicles
multiple loan	Only one loan at a time	Only one loan at a time
Sources of Fund	• Members Savings (in case of Islami Bank - depositors' savings) • PKSF	• Members' savings • PKSF • International donors
Future Trends	Expansion Financial viability Institutional strengthening	Expansion Financial viability Institutional strengthening

Source: This comparison is based on the author's findings of a field survey and interviews with 12 Secular and Islamic NGOs during the month of June 2002

Table A4.2.2: Categorization of MF-NGOs Based on Seven Criterion

Category	Average numbers of MF-NGOs	Active member	Total borrowers	Total savings	Cumulative disbursement	Total outstanding amount	Total RLF	Total credit staff
Small MF-NGOs	321	Up to 1,500	Up to 1,500	Up to 1,000,000	Up to 5,000,000	Up to 1,000,000	Up to 1,700,000	Up to 10
Medium MF-NGOs	238	1,501 to 15,000	1,501 to 20,000	1,000,001 to 15,000,000	5,000,001 to 120,000,000	1,000,001 to 20,000,000	1,700,001 to 37,000,000	11 to 90
Big MF-NGOs	51	>=15,001	>=20,001	>=15,000,001	>=120,000,001	>=20,000,001	>=37,000,001	>= 91

Source: CDF Statistics, VOL. 10,11, and 12 CDF, Dhaka

Table A4.2.3: Relative Performance of Small, Medium and Big MF-NGOs

Particulars	Small MF-NGOs		Medium MF-NGOs		Big MF-NGOs		Total MF-NGOs	
	Numbers of MF-NGOs	% of total	Numbers of MF-NGOs	% of total	Numbers of MF-NGOs	% of total	Numbers of MF-NGOs	% of total
Total active member	313	52.08	246	40.93	42	6.99	601	100
Total borrowers	404	67.56	168	28.09	26	4.35	598	100
Total savings	290	48.33	248	41.33	62	10.33	600	100
Total cumulative disbursement	312	51.91	231	38.44	58	9.65	601	100
Total outstanding amount	268	44.82	267	44.65	63	10.54	598	100
Total RLF	271	45.09	269	44.76	61	10.15	601	100
Total credit stuff	325	54.08	233	38.77	43	7.15	601	100
Average	312	51.98	238	39.57	51	8.45	600	100

Source: CDF Statistics, VOL. 10,11, and 12 CDF, Dhaka

Table A4.3.1: Composition of External Debt and Debt Indicators

	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02*
Total External Debt Stock (millions of US$)	2637.2	2999.3	3386.9	3515.8	3660.2	3664.4	3499.6	3580.0	3397.4	3606.3
Multilateral Debt (millions of US$)	1815.9	2156.1	2487.9	2655.2	2727.6	2826.9	2782.6	2936.4	2893.1	3032.9
Bilateral Paris Club (millions of US$)	281.8	332.0	380.2	350.6	346.0	324.5	288.3	260.6	131.5	180.3
Bilateral Non-Paris Club (millions of US$)	415.6	398.4	407.8	404.1	417.3	461.8	361.7	332.6	344.7	360.6
Commercial Banks (millions of US$)	17.1	1.3	7.7	3.0	1.0	2.5	5.4	3.0	6.0	3.6
Commercial Non Banks (millions of US$)	62.0	38.2	27.2	26.2	26.2	26.7	35.3	29.5	18.0	18.0
Other Loans (millions of US$)	44.8	73.4	76.2	75.9	74.7	22.0	26.3	17.9	4.1	10.8
Debt Service (millions of US$)	169.7	167.8	128.1	142.2	155.9	166.5	152.9	133.8	146.1	133.5
Accumulation of arrears out of current maturities (millions of US$)	46.2	17.1	19.9	35.3	20.8	27.4	52.8	29.3	4.7	0.3
Exports of Goods (millions of US$)	172.8	264.7	593.0	588.0	683.5	458.4	549.2	453.8	441.8	455.9
Exports of Goods and Non-factor Services (millions of US$)	253.5	200.3	664.8	723.3	837.5	633.9	734.4	650.3	629.5	649.3
Debt Indicators (Percentage)										
Multilateral debt as a % of total debt stock	68.9	71.9	73.5	75.5	75.9	77.1	79.5	82.0	85.2	84.1
Bilateral Paris Club as a % of total debt stock	10.7	11.1	11.2	10.0	9.6	8.86	8.2	7.3	3.9	5
Bilateral Non-Paris Club as a % of total debt stock	15.8	13.3	12.0	11.5	11.6	12.6	10.3	9.3	10.1	10
Commercial Banks as a % of total debt stock	0.6	0.0	0.2	0.1	0.0	0.07	0.2	0.1	0.2	0.1
Commercial Non Banks as a % of total debt stock	2.4	1.3	0.8	0.7	0.7	0.73	1.0	0.8	0.5	0.5
Other Loans as a % of total debt stock	1.7	2.4	2.2	2.2	2.1	0.6	0.8	0.5	0.1	0.3
Total External debt as a % of export of goods & services	1040.3	1497.4	509.5	486.1	437.0	578.1	476.0	549.6	525.8	555.4
Total External debt as a % of export of goods	1526.6	1133.2	571.2	597.9	535.5	792.1	636.6	787.1	749.3	791.1
Total external debt as a % of GDP	87.4	80.5	64.2	64.0	64.3	58.8	60.4	64.0	63.0	65.0
Total debt service as a % of export of goods and services	71.2	42.8	26.4	23.4	19.8	27.4	24.2	27.2	26.6	24.7
Total debt service as a % of GDP	5.2	3.6	2.7	2.6	2.6	2.7	2.0	2.2	2.3	2.2

*Projection; Source: Bank of Uganda and Ministry of Finance Planning and Economic Development

Table A4.3.2: Percentage Distribution of Uganda Central Government Recurrent Expenditure

Functional Classification	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02*
General Public Administration	28.7	26.7	30.5	27.1	27.1	28.1	14.8	22.6	33.4	25.7
Defense	15.1	17.2	20.1	20.3	19.5	19.8	24.4	25.9	22.5	17.3
Public Order and Safety	4.5	6.4	8.7	8.9	8.9	10.6	8.3	10.9	10.4	9.1
Education	11.9	10.3	11.0	9.7	9.9	10.6	9.2	14.8	11.6	8.0
Health	4.1	4.0	3.9	5.6	5.4	4.9	2.7	3.1	4.1	4.1
Other Community and Social Services	1.2	1.7	1.2	1.2	1.2	0.9	0.8	1.9	1.5	1.2
Agriculture	1.3	1.0	1.5	0.7	0.9	0.8	0.8	0.8	0.8	0.9
Roads	1.7	2.2	1.6	1.3	1.3	1.4	1.3	1.9	1.7	1.6
External Loan repayments &Interest	30.2	27.7	18.7	16.6	16.4	17.7	24.0	12.0	6.1	15.8
Other	1.3	2.8	2.8	8.6	9.4	5.2	13.7	6.1	7.9	16.3

Source: Background to the Budget (Various Issues)

Table 4.3.3: Percentage Distribution of Central Government Development Expenditure

	1988/89	1989/90	1990/91	1991/92	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98	1998/99	1999/00	2000/01	2001/02*
General Government	24.3	33.9	31.1	37.1	47.4	38.0	43.4	23.0	15.1	25.4	14.9	15.4	14.9	19.8
Defense	27.3	18.9	16.3	11.0	3.3	8.6	5.2	8.2	4.3	7.9	3.6	2.6	4.2	2.3
Public Order and Safety	4.1	4.1	2.9	4.5	4.5	10.1	4.7	5.3	3.1	2.5	4.2	3.1	2.4	3.4
Education Services	5.0	5.5	6.6	3.8	9.8	11.2	9.4	7.8	9.9	7.2	24.4	15.3	20.9	10.2
Health Affairs & Services	3.7	2.4	2.4	8.7	8.5	10.1	5.9	7.1	11.6	5.5	7.4	8.9	8.1	5.0
Community & Social Services	4.3	5.9	2.0	0.4	2.3	7.2	1.0	2.9	2.1	10.2	9.1	6.4	3.0	2.6
Economic Services	30.0	29.0	37.0	34.0	24.0	13.9	24.5	41.9	51.7	41.3	35.0	47.0	46.5	56.7
Other	1.2	0.4	1.7	0.4	0.2	1	5.8	3.9	2.1	0	1.3	1.4	0.0	0.0
	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0

Source: Background to the Budget (Various Issues)

Table A5.1: Net Financial Flows to LDCs:1996-2000

(US millions)

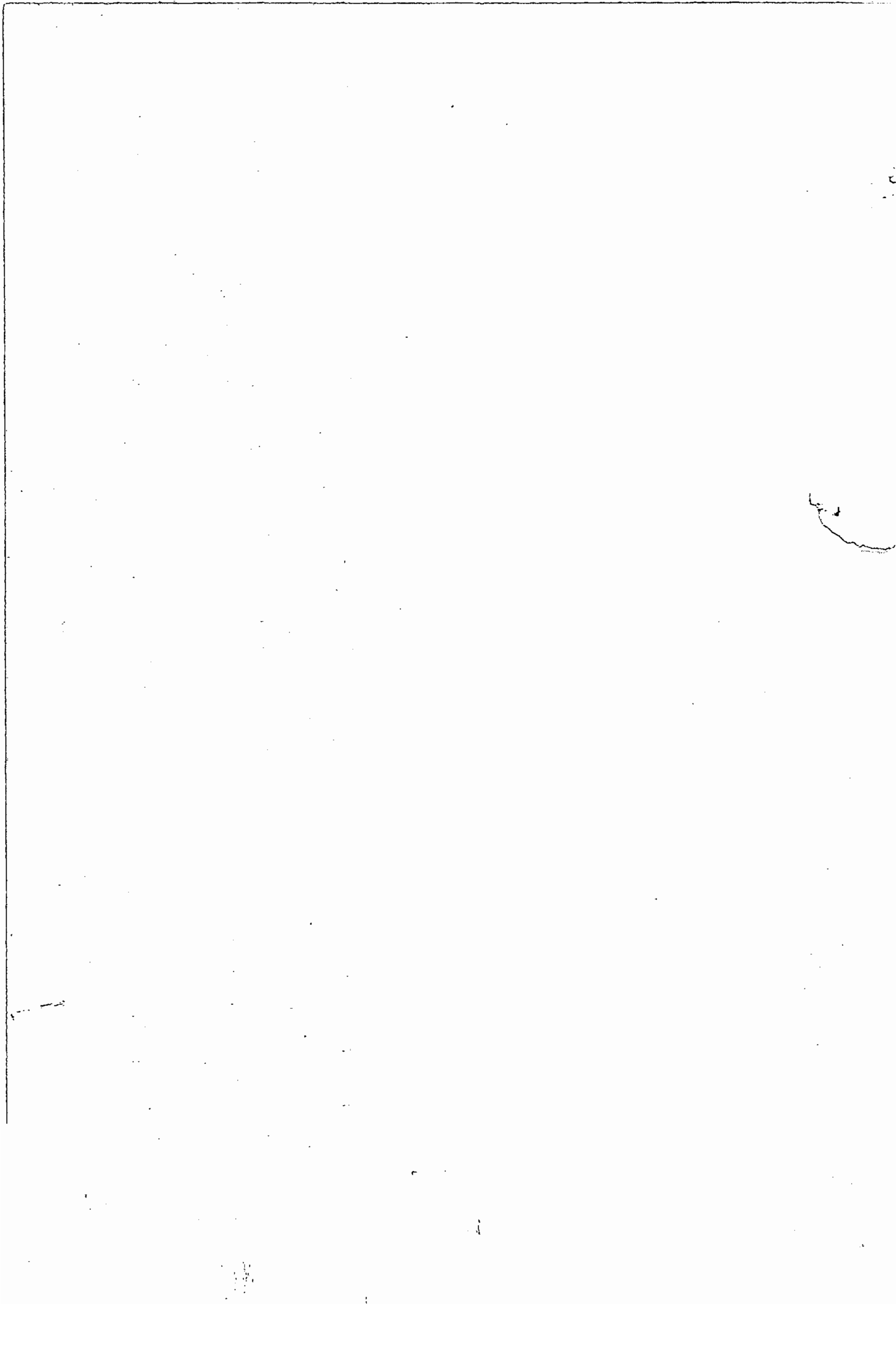
(ODA+OOF+Private)	1996	1997	1998	1999	2000
DAC Countries	8690.5	8865.3	9808.3	9076.5	8122.1
Multilateral					
AfDB	40.7	-21.3	-90.6	-72.2	-85.5
AfDF	446.7	443.4	403.3	326.4	203.5
AsDB	440.1	333.3	416	367.6	398.6
CarDB	.	.	.	.	.
EC	1392.9	1287	1350.5	1228.2	1001
EBRD	.	.	.	.	.
IBRD	-86.9	-64.8	-52.4	-38.2	-23.4
IDA	2082.8	1957.3	1605.6	1838.3	1770.6
IDB	36.2	44.2	56.2	49.2	26.4
IFAD	69.7	43.8	70.9	52.3	77
IFC	28.1	36.1	53.9	97.8	61.6
IMF	24.4	103.7	117.2	55.7	-2
UNDP	278.4	335.7	299.9	261	183
UNTA	60.9	95.2	61.9	99.7	110.2
UNICEF	308.3	162.4	147.8	159.1	168.4
UNRWA	.	.	.	.	.
UNHCR	124.3	116.9	100.2	103.2	171.1
WFP	237.1	149	139	202.4	213.6
Other Multilateral	192.7	93.6	99.2	80.9	133.6
Arab Agencies	.	.	.	.	.
Other Donor Countries	62.7	101.6	146.8	189.7	217.9
EC+EU Members	7324.1	7566.7	7949	6878.5	6052.5
Total	14421.3	14086.7	14736.7	14100.8	12760.7
GRANTS					
DAC Countries	7743.5	7369.7	7506.4	7149.1	7773.3
Multilateral	2510.3	2205.3	2344.9	2783.3	2172.1
Other Donor Countries	31.9	28.5	44.6	68.8	103.1
EC+EU Members	6303.5	5870.7	6080.8	5305.3	5594
Total	10285.6	9603.5	9895.9	10001.2	10048.5
Bilateral ODA Commitments (By Purpose)					
Social Structure &Services	2626.5	2389.2	2964.8	2677.8	2680.3
Education	629.6	773.4	810.4	657.2	755.8
Health&Population	645.7	585.3	672.1	775.8	718.1
Water Supply&Sanitation	449.3	334.5	358.7	345.4	271.2
Econ.	1437.2	1070.1	744.3	864	869.1
Transport&Communications	827.3	780.6	443.8	405.2	578.2
Energy	523.8	231.6	179	331.2	173.5
Production Sectors	964.2	738.3	677.6	638.2	830.5
Agriculture	799.9	659.6	587.7	521.6	670.5
Industry,	154.6	60.9	78.8	110.2	152.5
Trade&Tourism	9.7	17.8	11	6.4	7.5
Multisector	369.6	256.3	334.1	351	324.7
Program Assistance	864.5	818.3	1078	890.2	1508.1
Food Aid	409.5	480.1	487.3	649.1	526.3
Action Related to Debt	790.1	1059	1459.4	1061.9	1071.3
Emergency Assistance	600.4	545.3	619.7	768.3	900.2
Other&Unallocated/Unspecif	383.6	379.2	324.4	340.3	275.8
Total	8042.6	7257.9	8209.9	7607.1	8496.2

Source: Geographical Distribution of Financial Flows to Aid recipients 1996-2000, OECD.

Table A5.2: Net Financial Flows to Developing Countries:1996-2000 (US$. Millions)

(ODA+OOF+Private)	1996	1997	1998	1999	2000
DAC Countries	172620.2	170158.1	159703	173240.1	106885.3
Multilateral					
AfDB	291	-33.2	-196.7	-114.3	-303.6
AfDF	591.4	589.4	575.7	458.7	300.4
AsDB	1320	4980.7	5655.6	3516.5	1975.3
CarDB	1404	23.4	47	72.9	69.9
EC	5564.3	5992.4	5969.6	5548	4840.6
EBRD	395.4	260.5	342.9	229.3	241.5
IBRD	-238.1	3145.1	5745.5	3801.6	2775.9
IDA	5722.9	5253	4821.8	4508.9	4188.5
IDB	1814.7	2988.8	4440.2	6179.4	4513.4
IFAD	151.3	118	111.9	143.5	148.1
IFC	901.7	245.6	678.5	663.3	228.9
IMF	329.7	177.8	180.5	197.2	-88.5
UNDP	555.3	670.2	604.4	508.4	390.3
UNTA	242.6	434.3	282.1	428.4	454.5
UNICEF	677.1	513.7	483.7	564.5	576.4
UNRWA	236.8	263.5	298	286	300.8
UNHCR	281.1	261.1	235.8	252.9	492.5
WFP	371	278.7	269.5	355.7	357.3
Other Multilateral	797.7	336	392.6	384.5	739
Arab Agencies	.	.	.	.	.
Total	19984	26575.2	31158	28131.2	22377.9
Other Donor Countries	1092.4	1102.3	2092.5	872.9	580.7
EC+EU Members	83974.1	70239.4	89507.4	102736	75019.4
Total	193695.6	197835.7	192951.5	202244.1	129843.9
GRANTS					
DAC Countries	36533.8	31278	32476.2	33913.4	33022.2
Multilateral	8150.4	7491.9	7534.9	8243.3	7777.7
Other Donor Countries	589.3	546.3	515.5	392.7	615.7
EC+EU Members	24368.1	21471.6	21777.5	21576.6	19710.6
Total	45273.5	39316.1	40526.6	42549.4	41415.5
Bilateral ODA Commitments (By Purpose)					
Social Structure &Services	13133.4	11988.3	13754.6	14516.7	15228.7
Education	3672.6	3436.3	3191	4676.2	3489.5
Health & Population	2406.7	2332.8	2334	2231.7	2597.8
Water Supply&Sanitation	3332.2	2943.9	2514.7	2070.1	3032.2
Econ. Infrastructure&Services	11647.8	9155.2	8755.9	8143.7	7746
Transport&Communications	6927.6	4621.8	4296.6	4160.3	4474
Energy	3399.5	4010.4	2830.3	2109	1459.5
Production Sectors	5688.5	4621.9	3873.7	3532.5	3377.1
Agriculture	4232.8	3172	2929.8	2300.1	2285.3
Industry, Mining&Construction	1274.4	1350.8	772.9	1088.6	980.2
Trade&Tourism	181.4	99	171.1	143.8	111.7
Multisector	2297.7	1708.1	1682.3	2293.6	2785.5
Program Assistance	3284.2	2483.3	3739	3547	3804.2
Food Aid	877.5	1286.9	1167	1629.5	1425.7
Action Related to Debt	2804.7	2655.5	3628	2890.4	3209.6
Emergency Assistance	2901.1	2213.1	2999.3	6111	4076.9
Other&Unallocated/Unspecified	2159.4	2435.7	2920.5	3404.7	2195.2
Total	44296.9	37730.1	41826.2	45638.1	44745.5

Source: Geographical Distribution of Financial Flows to Aid recipients 1996-2000, OECD.



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