2. World Bank Group Strategic Approach

Reflecting resource-dependence in World Bank Group country strategies: All four countries included in this Clustered Country Program Evaluation (clustered CPE) depend heavily on the extraction of nonrenewable natural resources, and extractive sectors play a major role in their economies and public finances. Nevertheless, Bank Group strategies in these countries usually did not focus explicitly on the challenges more typical for resource-rich developing countries (RRDCs), including the role of natural resource revenues as a potential driving force for development and poverty reduction. A notable exception is the Country Partnership Strategy (CPS) for **Mongolia**, which—albeit somewhat belatedly—made the country's endowment with abundant mining resources the centerpiece of Bank Group strategic engagement. Mongolia also stands out in this cluster evaluation as the only country in which the Bank Group actually maintains direct engagement in the extractive sector through lending, analytic and advisory activities (AAA), and International Finance Corporation (IFC) investments. In the rest of the cluster, the Bank Group has been either effectively cut out of the sector, or was never involved in the first place.[1]

At the same time, Bank Group *de facto* engagement in the country program evaluation (CPE) countries, if viewed at the project and AAA levels, did offer solutions to the relevant challenges in the areas where the Bank Group has a comparative advantage, that is, macroeconomic management, infrastructure investment, human development, and so on. Oftentimes, the Bank Group used openings offered through successful AAA to introduce lending and project implementation support.

The country context dictated the prominence of issues related to resource use in the Bank's strategy. The visibility and prominence of the natural resource (NR) factor in country strategy documents generally reflected the quality and depth of overall dialogue with the respective government authorities. For example, **Bolivia**'s policy in the hydrocarbon sector, including the 2005 Hydrocarbon Law and the nationalization in 2006, proceeded independently of Bank Group advice. The 2006 policy notes prepared by the Bank Group argued against the direction in which Bolivia's natural gas policy had gone and was about to go even more extremely. As a result, since 2006 the government has not sought any help from the World Bank Group on hydrocarbon sector issues. The Bank Group strategy in **Zambia** implicitly recognized the challenge of extremely high dependency on natural resources, and especially the country's vulnerability to the effects of copper price volatility, which made macroeconomic and fiscal management extremely challenging. However, in the Zambian context many of the questions related to the use of resource revenues had little relevance. Instead, the

key question was whether the Bank could have done more to assist the government in maximizing revenues, specifically: copper accounted for about 80 percent of exports, but only 4 percent of fiscal revenue. The Bank faced a dilemma: whether to support the renegotiation of the mining contracts or maximize revenue collection within the limits of the existing contracts. The issue was highly sensitive as the Bank did share some responsibility for the contracts negotiated with the privatized mines. These contracts did not include a provision for capturing windfall profits in the event of a rise in copper prices. In hindsight, the Bank could have made an earlier start (in a much more favorable country dialogue climate) on the current agenda to strengthen the capacity of the Ministry of Finance to analyze company accounts and to identify inappropriate use of transfer pricing, write-offs, and depreciation allowances.

IFC does not have an explicit strategy for its operations in RRDCs. Instead, it has a sector strategy for engagement with extractive industries. Despite attractive investment returns, IFC considers extractive industry a "high-risk" business. Due to the combination of high risk and fairly intensive staff needs to structure a transaction, IFC also considers the extractive industry a low-volume business in which it should be highly selective and seeks to optimize both development and financial results. Considering the potential reputational risk for IFC, governance is one of the most important risk factors. For higher risk countries that do not have an established track record of regulatory oversight for the sector, IFC's strategy is to work closely with the World Bank. However, this evaluation found that coordination between the Bank and IFC was ad-hoc and not systematic. CPSs seem to be joint in name only, with weak sector analysis. Both the Bank and IFC generally failed to establish a long-term sector engagement and effective implementation strategy for joint contributions to the CPS and sector objectives. Apart from some pockets of success, IFC struggled to do business in the four CPE countries beyond its main business line of banking and the financial sector. In the four CPE countries, IFC had rather limited engagement in infrastructure, where it has a comparative advantage and global expertise in providing long-term financing and advice on public-private partnerships (PPPs).[2] In **Bolivia**, despite a growing economy supported by a booming small and medium enterprise (SME) sector, IFC experienced difficulties in finding long-term investment opportunities in general.

Quality of dialogue: RRDCs have substantial resources to fund government programs, and are therefore less dependent on donor funding. Their willingness to engage in a dialogue is often dependent on the establishment of a shared vision and mutual trust. Bank Group strategies generally aligned with the governments' development plans. However, very often the overarching objective was to build (or, at times, re-build) a strategic relationship with the authorities. Dramatic positive changes in the macroeconomic situation due to commodity price booms, and the governments' often critical view of the international financial institutions negatively affected the extent and

form of Bank Group engagement in **Bolivia,** and to a lesser extent in **Zambia**. In this context, the Bank Group often chose to "re-invent itself" and offer unconventional mechanisms of cooperation—albeit with varying success. The Bank Group had more success with this approach in **Kazakhstan** where, after a considerable hiatus in its program, it developed two effective mechanisms of dialogue. These included the regular rounds of cabinet-level "brainstorming sessions" prepared and led by the Bank and chaired by the Prime Minister, and the Joint Economic Research Program (JERP). The JERP was a demand-driven, co-funded program of analytical studies and policy notes on specific sector topics. Implementation of the JERP in Kazakhstan offers some interesting lessons: while it became a powerful tool for strengthening the partnership, advancing the reform agenda and a gradual build-up of the lending program, the fully demand-driven nature of the program imposed limitations on the Bank in defining strategic priorities in its advisory work, disseminating AAA findings, and engaging with local partners.

Tension between the Bank's mandate and the government's preferences with regard to the Bank's assistance program was a common characteristic for resource-rich countries in which the clients did not need the Bank's financial support. Thus, they could afford to be very selective, including in the use of Bank policy advice. In **Bolivia,** following the transition to the Morales government in 2005–06, the Bank lost its traditional influence on policy, and worked hard to "stay engaged," exploring entries for dialogue with a publically antagonistic client. The Morales government has been largely uninterested in the Bank's advice on macroeconomic policy, governance, and resource extraction. In this context, the Bank chose to focus on other areas of engagement. The program became increasingly opportunistic and narrow in scope, reflecting an engagement with areas of support selected by the government, but not necessarily coherent or suitable for achieving the intended results. While possibly appropriate for a transitional period, this strategy may no longer be viable as the Bank could incur reputational risk.

Pro-active engagement with legislatures proved quite useful, especially in countries with growing traditions of parliamentary democracy, such as in **Mongolia.** In Mongolia, the Bank crafted an outreach effort to engage members of parliament in order to build majority support around policy reforms, strengthen the management of the mining sector, and target social welfare reforms. This helped the Bank to stay engaged in dialogue in a society prone to drastic political changes after each electoral cycle that, in turn, led to deep divisions on important issues, thereby imposing challenges to implementing a sustainable reform agenda. Increased country and sector presence was another positive factor: the establishment of a country director-led office in Lusaka, **Zambia** demonstrated the Bank's commitment to building a robust relationship with Zambian authorities. The placement of a senior mining specialist in Ulan Bator helped to strengthen engagement in this critically important sector for **Mongolia.** In **Zambia**

and **Bolivia**, the lack of dedicated IFC staff resources and presence in the country hindered effective cooperation between the Bank and IFC.

In countries with active electoral politics, and thus frequent and unpredictable changes of government, the interaction of politics and mineral cycles can lead to systematic problems that spill over into country–Bank relations. At times when a country has few mineral revenues coming in—either because world prices are low or the minerals are not yet being exported—then the country is in a weak position vis-à-vis international oil and mining firms. Such firms can drive a hard bargain in contracting for exploration and extraction. Also, at these times the government is likely to depend on the Bank's blessing to obtain financing, leading to "close collaboration" in policy dialogue. In the next phase of the commodity price cycle, with extraction investments already in place and buoyant world prices, it often looks like the exploration and extraction contracts were bad deals for the country. The Bank can be portrayed as the advisor that led the previous government to give away too much. That happened in **Bolivia**, and to a lesser extent in **Zambia** and **Mongolia**.

Political economy analysis: In all of the reviewed countries, a good understanding of the political economy of natural resources was absolutely critical. Governments tend to use mineral resources as tools in promoting their respective political agendas. The discovery of large mineral resources often contributes to more fiercely contested elections and unstable governments, and attendant highly populist decision making aimed at winning constituencies through distribution of the new wealth (World Bank 2012). The Bank's ability to take a longer view, to maintain a consistent presence, and to exploit the synergies between its various operations is important to be able to mitigate the populism that dominates decision making in many RRDCs. With this perspective, the Bank could be an important contributor if and when economic populism ceases to dominate policy making. In **Mongolia**, Bank-sponsored political economy analysis proved to be a key input in identifying the constraints to adopting policies for the effective management of revenues from the mining boom (World Bank 2009). The findings of the political economy analysis showed the importance of enhancing information and stimulating multi-stakeholder debates about the governance of the mining sector. The analysis helped identify the key actors, notably the powerful political factions that advocated or opposed different facets of the reform program. Because resource cycles can precipitate the decision-making process without sound analysis, the country team devised a comprehensive outreach effort to engage stakeholders in government, the parliament, and civil society. In **Zambia**, the Bank produced a study on revenues from mining (2011) and a political economy analysis that, among other things, warned against industrial policy approaches to diversification and against repeating the experience of creating parastatals in the 1970s and 80s.

Increased role of AAA: Rapidly decreasing demand for Bank Group financing in most RRDCs during the review period accorded a more prominent role to the Bank Group's AAA work. In **Bolivia**, the number of AAA products delivered during the period more than doubled compared to the preceding decade. Analytic work became an increasingly convenient tool to stay current on developments in many areas and to respond to the government's requests for assistance on specific topics. **Kazakhstan's** JERP is a good example of a well-established and effective mechanism in this regard. At the same time, the overall effectiveness of the JERP did suffer from the absence of an explicit results framework and the lack of detailed evidence on how much and what kind of Bank policy recommendations resulted in policy changes. The Bank rarely monitored the results of its recommendations, while the government's own monitoring was sporadic and not regularly shared with the Bank. In **Zambia**, this evaluation found much stronger interest in the Bank's analytic work than had appeared from earlier assessments **(**2004). A series of semiannual Country Economic Briefs in Zambia were a very useful innovation and an instrument of choice to which officials, academics, think tanks and civil society organizations looked to obtain objective analysis of the current economic situation. The Bank's periodic economic reports in **Mongolia** became a cornerstone of the Bank's communication policy, helping to raise awareness about economic trends and providing the opportunity to discuss frankly the risks posed by countercyclical government policies.

Capacity building: While capacity building is a common and generic "buzzword" across the whole range of Bank clientele, RRDCs have a few special needs in this regard. Negotiating capacity is one of them. **Botswana** is an excellent example of the importance of investing in this function, as the outcomes of its long-term deal with the country's main investor (De Beers) clearly show. By all accounts, the country did not spare efforts and resources to build an equally qualified team on the other side of the negotiating table, and this investment had a high payoff.[3] One of the key lessons that emerges from the Bank's support in **Zambia** is the importance of ensuring that the country has the right expertise available at the negotiation stage of mineral contracts and privatization. The failure to look at other fiscal regimes and obtain expertise on appropriate taxation arrangements has had negative consequences for that country. In **Kazakhstan**, building local analytical capacity was a dimension that did not live up to its potential. The JERP very rarely (if at all) engaged local partners in program delivery. As such, the 10–year old program of analytical studies contributed surprisingly little to the build-up of local analytical capacity. In **Bolivia**, the Morales government thought that the Bank had been complicit in the favorable deals that international oil companies had negotiated with previous governments. Consequently, it sought non-Bank expertise to design the new hydrocarbon law, which was less favorable to the international firms.

Partnerships and the demand side of reforms: Experience in all countries proves the importance and crucial role of building and nurturing long-term partnerships and communication with all major stakeholders, also moving beyond the usual and main counterparts of the executive branch of government. This should include the legislature, private sector, civil society, academia, and donor partners. The Bank's early (pre-2005) engagement in **Bolivia** focused on working with the government and overlooked building partnerships with other stakeholders. This later backfired, leading to animosity toward and distrust of the Bank by many Bolivians, including the Morales government. The Bank Group's subsequent and recent approach of not antagonizing the current administration in any way has also been criticized as evading its role as an unbiased source of knowledge and a trusted development partner. By contrast, in **Mongolia**, the Bank used the recommendations of political economy analysis, and came up with a comprehensive program of outreach and capacity building with the media, parliament, and civil society. The effectiveness of the Bank's program in **Kazakhstan** was reduced by the lack of attention to demands from civil society and the private sector. The Bank's policy dialogue focused exclusively on the government at the cost of not communicating with other local stakeholders. Most importantly, limited disclosure kept important policy recommendations out of the general public's reach, thus constraining demand for reforms, and adversely affecting the political economy of governance reforms in the country.

Selectivity: In the context of RRDCs and shrinking demand for Bank services in some sectors, selectivity becomes an obvious strategic imperative in order to stay current and relevant. This refers particularly to the Bank Group's loans and investments. Bank Group strategies do recognize this and, indeed, call for increased selectivity and focus in Bank Group interventions—although in many cases selectivity has been defined by the authorities. While this is generally natural and logical, and all development initiatives should be client-driven and owned, there is one major caveat. In some countries, this client-led selectivity has led to the Bank's *de facto* withdrawal from providing impartial advice on important but politically sensitive areas, such as poverty diagnostics, macro-fiscal management, and governance. In these cases, the Bank should stay cognizant of its mandate as a global development agency and the immediate risks facing many RRDCs, such as the looming deterioration of fiscal balances (already happening in **Zambia** and **Mongolia**) amid falling commodity prices that will create serious risks for countries dependent on mineral exports.

Flexibility: Flexibility is especially important in resource-dependent countries, given the potential for price shocks and the ensuing variability in revenue. Bank strategy was generally flexible in design and practice in all countries. The increasing prominence of technical assistance in the overall program was an important contributing factor in this regard, as it enhanced Bank capacity to adjust to quickly evolving priorities. In

Mongolia, the Bank team reacted promptly to realign the Bank portfolio to help the government cope with the global economic crisis in 2008–09. It did so by shifting the majority of new International Development Association resources to development policy credits, and intensifying the AAA emphasis on real-time policy advice. The Bank Group's "open-ended" 2004 CPS in **Kazakhstan** was designed as a flexible strategy instrument that would allow for quick mid-course correction—which, indeed, happened at the time of economic and financial crises. However, flexibility of the program should not explain and justify the absence of concrete and measurable performance indicators that limited the ability to measure actual progress and achievements.

Overall, looking at the four resource-rich countries in this evaluation, one does not see the World Bank Group as having a consistent framework or core set of issues to include in the dialogue with resource-rich countries. Each of the four stories evolved in a unique way that depended on how the country team at the time decided to react to differing country circumstances. The Bank's responses did not seem to derive from any Bank-wide approach to working with RRDCs. The mineral wealth affected country dialogues as the Bank Group adapted its strategy to the situation, but this was usually more in a negative way of limiting the issues that entered into the dialogue. At the same time, this evaluation argues that despite all the differences between the countries included in the cluster, there were common challenges and opportunities where the Bank Group and its clients can learn across countries and Regions, and come up with solutions to some of the toughest development challenges facing this particular group of Bank Group client countries.

References

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[1] Bank Group direct financial engagement with extractive industries is quite low globally, and the total financing volume for the last decade was only $9 billion—less than $1 billion annually worldwide (mainly IFC equity investments). In the four reviewed countries, IFC has made one small investment in a junior mine in Zambia and another in Mongolia for the Oyu Tolgoi copper–gold mine in the amount of $4.5 billion, approved by IFC and the Multilateral Guarantee Agency's Boards on February 28, 2013. The financing was not yet finalized at the time this report was prepared due to continuing negotiations on key issues between the investors and the government.

[2] IFC had only one infrastructure investment in the four CPE countries—a $50 million project in Kazakhstan. This report and the CPEs use the IFC information system classification of infrastructure investments. This will not include telecom, IT, and oil and gas sector investments.

[3] Botswana has negotiated an increasing share of the profits from diamond mining, in 2015, about 81 percent. It also reached an agreement with De Beers to move an increasing share of value-added (through polishing and processing) to Botswana, as well as its headquarters from London to Gaborone. Botswana is a 50 percent shareholder in Debswana, the world's leading producer of diamonds by value, and the Diamond Trading Company.