

# **Good Governance and the World Bank**

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## Executive Summary

The World Bank's 'good governance' agenda is concerned with the relationship between the state, the market, and civil society in loan-receiving countries. The ideal of the 'minimalist state' has been replaced with that of the 'effective state'. The Bank argues that in order to be effective, the state must play a critical role in managing and regulating the market and civil society. This briefing paper looks in detail at the Bank's conception of 'good governance', examines how it has been implemented in practice, and identifies some of the tensions underlying the governance agenda.

The first section charts the rise of the good governance agenda and the Bank's new focus on the state and institutions. We then turn to look at the promotion of legal reform and anti-corruption measures in loan-receiving countries. The Bank is seeking to establish well-functioning market economies with stable property rights, enforceable contracts, high levels of transparency, and low levels of corruption. The creation of effective institutions is seen as a counterweight to arbitrary state action, and like the democratization and participation agendas, this is a previously uncharted area for the Bank. However, the Bank's market-centric approach and unwillingness to fully consider the role of political factors in corruption and legal reform has sometimes resulted in inadequate or inappropriate reforms.

We then look at World Bank policies and activities in the key areas of macroeconomic policy reform, financial sector strengthening, and privatization. The relationship between the state and the market lies at the heart of the World Bank's good governance agenda and the Bank has undertaken many reforms in this area. Despite the move to institutions, neo-liberal policies still dominate the Bank's philosophy, leaving the good governance agenda market-centric rather than state-centric. The report finds that the Bank's faith in market mechanisms underestimates the significant challenges posed by institution-building and the need to protect the vulnerable.

The final section examines good governance in state-civil society relations, looking in depth at attempts to promote participation, democratization, and decentralization. Significantly, the Bank's Articles of Agreement restrict it from addressing 'political' issues in its lending activities, meaning that in the past, issues such as democratization and, to a lesser extent, decentralization, were largely absent from its agenda. By contrast, the Bank's Comprehensive Development Framework embraces the idea of civil society participation in development. What participation means in practice and how far the Bank's commitment to civil society really extends, however, is ambiguous. The Bank is caught between its neutral mandate and pressure to address 'political' issues.

In sum, the good governance agenda marks a welcome change from the narrow market orthodoxy of the 1980s. As it stands, however, the governance agenda is far from perfect. Institutions are by nature political, social, cultural and economic entities; as such, the task of developing and sustaining them must be grounded in a dynamic conception of development. The conclusion argues that this requires a more fundamental re-evaluation of the role of the Bank, its philosophy, and self-governance than the 'good governance' agenda has provided so far.

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## 1. Introduction

The concept of ‘governance’ has a long and distinguished pedigree. From the Greek city-state to the modern nation-state, governance—or the art of governing—has been a constant preoccupation for rulers and political philosophers. In recent years, the idea that ‘governance matters’ has become a global theme. In the 1990s, aid donors and a range of international institutions, including the multilateral development banks, the International Monetary Fund (IMF), the Organization for Economic Cooperation and Development (OECD), and the United Nations Development Program (UNDP), formally adopted ‘governance’ agendas.<sup>1</sup>

There are many competing views on what the term ‘good governance’ should mean, but most donors argue that it should include some (if not all) of these: increased public accountability and transparency; respect for and strengthening of the rule of law and anti-corruption measures; democratization, decentralization and local government reform; increased civil-society participation in development; and respect for human rights and the environment.<sup>2</sup>

As a development institution, the World Bank has always had a vision of good governance, but three aspects of its current agenda are new. First, the Bank puts great emphasis on the need to change developing countries *from within*. The good governance agenda explicitly recognises that aid cannot be effective in the absence of a ‘good policy environment’.

Second, the current good governance agenda identifies a positive—albeit restricted—role for the state and institutions, in contrast with its pro-market stance of the 1980s. During that period, structural adjustment loans were designed to reduce state intervention in developing-country economies. In the 1990s, the central Bank paradigm changed from ‘getting the prices right’ to ‘getting the institutions right’. Although extending the reach of the market remains at the core of the Bank’s vision, this view is tempered by the recognition that the state can play an important role as the provider of institutions for the market.

Third, the good governance agenda has led the World Bank into previously uncharted territory, such as the issues of participation, corruption, and democratic reform. Although the exact direction of Bank policy in all these areas remains ambiguous, the good governance agenda has undoubtedly stretched the Bank’s traditionally ‘technocratic’ character to a greater extent than ever before.

The Bank’s adoption of the good governance agenda raises critical questions about the organisation’s role in the development process and in the system of global governance as a whole. Aside from the rhetoric, what sort of governance has the Bank promoted in practice? Does the good governance agenda mark a real break with the neo-liberal policies of the 1980s, or is good governance merely the old ‘Washington consensus’ in new clothes?

More fundamentally, to what extent is the ‘good governance’ agenda compatible with the Bank’s founding mandate? The Bank’s Articles of Agreement prohibit it from interfering in the political affairs of member states. Article IV, Section 10 reads, ‘the Bank and its officers shall not interfere in the political affairs of any member; nor shall they be influenced in their decisions by the political character of the member or members concerned.’<sup>3</sup>

The Bank was founded as a technocratic organisation dedicated to the promotion of European reconstruction, rather than an organisation driven by a specific ideological agenda. But governance—which is concerned with the distribution of power and resources—is by its very nature a ‘political’ concept. Indeed, the World Bank originally defined governance in explicitly political terms, as ‘the exercise of political power to manage a nation’s affairs’ (a definition which was later abandoned).<sup>4</sup>

Attempting to steer a course between the political aspects of ‘good governance’ and the apolitical mandate, the Bank’s General Counsel suggested that ‘governance’ would be within the Bank’s mandate if restricted to the promotion of order and discipline in the management of a country’s resources.<sup>5</sup> Four areas were originally identified as being consistent with this definition: those of public sector management, accountability, strengthening the legal framework for development and the provision of information and transparency.

In practice, though, the governance agenda has undoubtedly involved the Bank in ‘political’ issues. This raises the question, should the Bank be addressing governance at all? One line of reasoning is that the Bank could never have been a ‘technocratic’ organisation in the first place. Given that its activities already stretch beyond its original Articles—which contain no reference to poverty alleviation, for example—the adoption of a good governance agenda can be seen as the logical next step. Critics argue that it is impossible for the Bank to attempt to alleviate global poverty without addressing issues such as respect for human rights.

Even if the Bank’s involvement in governance is deemed legitimate, however, how useful is the Bank’s move to addressing governance issues, and does it possess expertise in this area? As one author puts it, the challenge is to ‘move from axiomatic claims about the importance of institutions to more systematic analyses of institutional quality and its implications for various aspects of well-being’.<sup>6</sup> Has the Bank managed to develop successful strategies for implementing good governance reforms?

With respect to implementation, one controversial issue is the extent to which good governance can be defined and measured. The World Bank has undertaken extensive research into areas such as institutional quality, governance, corruption and so on.<sup>7</sup> This research relies on indicators of good governance, such as: voice/accountability, political stability, government effectiveness, regulatory quality, the rule of law, and control of corruption.<sup>8</sup>

Indicator-based systems are not fail-safe, however. Measuring governance is problematic because it is rooted in qualitative as well as quantitative factors and thus involves making value judgments. Indicators do not necessarily translate well across cultures and political systems: what seems corrupt in one society might not seem corrupt in another;<sup>9</sup> pollsters may interpret the data subjectively and exaggerate findings;<sup>10</sup> informants might provide faulty or confusing information; polls might be selective for commercial reasons,<sup>11</sup> and so forth.

Good governance conditionality is another controversial implementation issue. Conditionality, or the attaching of conditions to loans, has played a key role in the implementation of the good governance agenda.<sup>12</sup> The objective of governance conditionality is to exert pressure on borrowing countries to improve their policies and thus enhance the effectiveness of aid. During the course of the 1980s the number of good governance conditions attached to World Bank loans

rose dramatically, from an average of 21 conditions per loan in 1980, to 55 by 1990, falling gradually to 33 average conditions per loan by 2000.

### WORLD BANK CONDITIONALITY 1980-2000<sup>13</sup>

Financial Year	Average no. of conditions	
	All conditions (including nonbinding actions)	Legally binding tranche release conditions
1980	21	12
1985	34	19
1990	55	34
1995	53	37
2000	33	25

The use of governance conditionality is beset with problems, however. The use of conditionality has met fierce resistance from recipient countries, and a number of studies show that it has been ineffective.<sup>14</sup> This ineffectiveness derives in part from the vagueness of the concept of good governance itself, and from the fact that there is a real confusion at the heart of the governance agenda about whether governance is a *precondition* for successful development or development's *objective*.<sup>15</sup> If good governance is a precondition for the implementation of reforms, should the World Bank lend selectively to those countries that already demonstrate the basics of good governance? And if so, how should the Bank deal with badly governed states?<sup>16</sup>

The difficulties surrounding the use of conditionality can be taken as a metaphor for the problems and ambiguities plaguing the good governance agenda in general. At root is a fundamental dilemma, the extent to which it is feasible and legitimate for the World Bank to become deeply involved in the everyday governance of developing states. This report attempts to shed light on some aspects of the Bank's role by presenting a broad analysis of the theory and practice of the governance agenda.

## 2. Governance and Institutions

The Bank has defined 'good governance' as 'the manner in which power is exercised in the management of a country's economic and social resources for development'.<sup>17</sup> The governance agenda is concerned with reforming the relationship between government, civil society, and the market in recipient states. In the spirit of the Comprehensive Development Framework (CDF), the Bank perceives a symbiotic relationship between the three sectors: the state, for example, can regulate the market and provide a firm legal foundation for business; and civil society, by means of bodies such as the independent media, can keep a check on the state.

The figures look impressive on paper: since 1996, the World Bank has set up over 600 governance-related programmes and initiatives in 95 developing countries, and has also supported governance and public sector reform programs in 50 countries.<sup>18</sup>

Why this new interest in promoting good governance? Geopolitical factors, such as the end of the Cold War, played a part, but the primary cause was the failure of structural adjustment programmes in developing countries in the 1980s, and 'shock therapy' in post-communist

countries in the early 1990s. For example, despite granting multiple adjustment loans to countries in Africa, Latin America and Asia, the per capita growth rate of a typical developing country between 1980 and 1998 was zero.<sup>19</sup> Neo-liberal policy reforms halved the Russian GDP and increased inequality two-fold between 1989 and 1996.<sup>20</sup> The negative impact of structural adjustment was criticised in a number of high-profile reports (see table below).

### **Key milestones in the World Bank discourse on governance**

1989 *Sub-Saharan Africa: from Crisis to Growth* identifies a ‘crisis in governance’.

1993 *The Wapenhans Report* criticises structural adjustment policies for paying too little attention to institutional and political factors.

1992 *Governance and Development* argues that good governance is central to creating and sustaining an environment which fosters strong and equitable development, and it is an essential complement to sound economic policies.

1997 *World Development Report - The State in a Changing World* acknowledges the crucial role of the state as central to economic and social development.

1999 *The Comprehensive Development Framework (CDF)* is announced, emphasising the inter-dependence of institutions and the human, physical, social and macroeconomic aspects of development.

2002 *World Development Report - Building Institutions for Markets* identifies how institutions can promote the private sector and provides policy guidance on how to build them.

Bank staff blame the failure of structural adjustment on ‘poor governance’ in developing and transition countries. By this, the Bank means the presence of inadequate legal frameworks, inefficient financial systems, insufficient regulatory mechanisms, excessive political interference, and widespread corruption in developing countries. Although getting macroeconomic policy right remains fundamental, the Bank has argued that more attention must be given to creating the *preconditions* for market economies; neither good policies nor investment can be sustained in an environment with dysfunctional institutions.<sup>21</sup> In short, the good governance agenda entails an explicit recognition that the *quality* of governance is a determinant for aid effectiveness.<sup>22</sup>

In theory, the governance agenda marks a watershed in the Bank’s approach to the role of the state and institutions. The 1997 World Development Report, *The State in a Changing World*, acknowledges that the state has a critical role to play in promoting development, in direct contrast to its pro-market policies of the 1980s. The report envisages the state ‘not as a direct provider of growth but as a partner, catalyst, and facilitator.’<sup>23</sup> In other words, the state should focus on upholding the rule of law, promoting competition, and regulating the financial system, while avoiding excessive intervention in the economy. Intervention, the Bank argues, will discourage corruption and encourage investment.

The 2002 World Development Report, *Building Institutions for Markets*, develops this view further. The report argues that the World Bank can help developing countries to build institutions (often defined as ‘formal and informal rules and their enforcement mechanisms that shape the behaviour of individuals and organisations in society’<sup>24</sup>) that develop markets, promote growth, and facilitate access. The report argues that while markets provide the best means of achieving growth and reducing poverty in the long term, the problem is that markets often don’t work—for example, by failing to provide adequate incentive structures. In other words, ‘good policies are not enough’; good policies must be backed up by sound institutions in order to have a positive impact.<sup>25</sup>

### Examples of Market-Supporting Institutions<sup>26</sup>

#### *Public*

Judicial systems  
 Competition laws  
 Bank supervisory authorities  
 Disclosure requirements on companies  
 Formal land titles and inheritance laws

#### *Private*

Chambers of commerce  
 Credit reforms  
 Moneylenders  
 Reciprocity among business partners  
 Land inheritance norms

According to the Bank, institutions have three important benefits. First, institutions such as accounting firms, credit regimes, and government regulations channel information about market conditions, goods, and participants. Second, institutions such as constitutions and judicial systems define and enforce property rights and contracts, determining—as the Bank puts it—‘who gets what and when’. Third, institutions have the ability to increase or decrease competition in markets. Increased competition is desirable, according to the Bank, because it increases quality: ‘competition among jurisdictions highlights successful institutions and promotes demand for them. Competition among firms and individuals does the same.’<sup>27</sup>

Adopting the good governance agenda has thus entailed re-defining the Bank’s position on the desirability of the state and institutions. It now emphasises the idea that states and markets are *complementary* rather than competitive, and that efficient markets and efficient states are required for economic growth and development. Rather than hindering development, the state can play a key role in managing, regulating and monitoring the private sector. In turn, the private sector, by taking over the provision of public services wherever possible, relieves the burden on the state and provides more efficient services.

Despite this new interest in institutions, however, in the Bank’s view the market remains the engine of growth and sustainable development. As the 2002 World Development Report puts it, ‘the challenge for policymakers is to shape institutional development in ways that enhance economic development.’<sup>28</sup> The Bank claims that this is compatible with its anti-poverty agenda: the combination of market-led development with sound institutions, it is argued, will empower the poor.<sup>29</sup>

### **3. Promoting sound institutions: legal reform and anti-corruption measures**

Respect for the rule of law and for norms of social and economic behaviour is central to the World Bank's vision of good governance. The extent to which the rule of law is upheld and corruption controlled serve as indicators of crime levels, of the effectiveness and predictability of the judiciary, and of the enforceability of contracts; in short, levels of stability and predictability in a given society.<sup>30</sup> Stability and predictability, in turn, are essential preconditions for private sector development and participatory relations with civil society.

The Bank's own literature highlights the need to 'get the institutions right'. Experience suggests that sound legal institutions are a fundamental part of the institutional architecture of any country. Outsiders are unlikely to invest in a state that is unable to uphold the rule of law. As one Bank spokesperson has noted, 'it took the failures in governance and development in Africa, the collapse of dictatorships in Latin America and the great transformations of Central and Eastern Europe to recognise that without a sound legal framework, without an independent and honest judiciary, economic and social development risk collapse.'<sup>31</sup>

#### **3.1 Legal Reform**

The practice of promoting the rule of law abroad has a long history. In the 1960s, USAID and various private American donors launched a 'law and development' movement to reform the judicial systems and laws of developing countries in Asia, Africa, and Latin America. Law improvement was seen as an essential building block of social reform. The movement suffered many setbacks that were blamed on a multitude of factors, such as the fact that the movement attempted to 'transplant' American legal culture; the exclusion of informal legal mechanisms; and inadequate efforts to ensure country participation.<sup>32</sup>

In recent years, legal reform has enjoyed a revival,<sup>33</sup> and the World Bank has played a major role in promoting legal reform as part of its good governance agenda. In early projects, the Bank focused on administrative and management reforms and judicial training, initiatives that were essentially technocratic in nature. More recently, the scope of the legal reform agenda has broadened to include issues such as judicial autonomy and ensuring better access to justice.

The World Bank has been involved in lending and non-lending activities. The latter typically involve knowledge sharing, capacity-building and assessment of countries' legal and judicial systems. At the same time, the Bank has supported legal and judicial reforms in a variety of lending instruments and in a wide range of lending operations. In many cases, legal reform has been a component of larger reforms aimed at capacity-building and institutional development. The Bank has also supported 'freestanding' legal and judicial reform projects (projects exclusively devoted to legal and judicial reforms).

**Table: the Bank's involvement in legal reform activities by 2001**<sup>34</sup>

Activity	No.
Freestanding project	17 (13 more in the pipeline)
Specialised legal assistance	87 countries, 45 areas

### *The role of legal reform in development*

Legal institutions can act as significant counterweights to the state, and the Bank is particularly interested in using legal reform to restrain arbitrary state action. One report argues that ‘the judiciary [is] in a unique position to support sustainable development by holding the other two branches accountable for their decisions and underpinning the credibility of the overall business and political environment.’<sup>35</sup>

The Bank argues that law plays a crucial role in promoting *economic* development: it creates certainty and predictability; it lowers transaction costs; it accords greater access to capital; and respect for the rule of law helps to establish a ‘level playing field’ for the private sector.<sup>36</sup> Leading legal scholars within the Bank have also suggested that the judicial system serves as a mechanism for conflict resolution, limits the threat of arbitrary political interference, and provides laws for safeguarding business interests and enforcement of contracts.

More recently, the Bank has also argued that law plays a role in promoting *social* development.<sup>37</sup> The Bank’s 2001 Annual Report, for example, argues that the harnessing of legal rights is one means of empowerment for the poor. Law enables the poor to take advantage of opportunities while protecting themselves against inequitable and arbitrary treatment.

The advantage of the legal reform agenda, in the Bank’s view, is that it is a seemingly neutral means of improving countries’ prospects for development. In order to avoid possible accusations of political bias, though, the Bank restricts its project undertakings to those which are interpreted as directly promoting economic and social development *and* requested by an interested borrowing member country. The Bank also attempts to avoid ‘political’ debates about the allocation and distribution of resources. Laws regulating economic affairs are deemed ‘political’ while efficiency-enhancing rules and regulations are not.

### *Issues arising from the legal reform agenda*

The failures of the 1960s legal reform movement do not bode well for the success of the current good governance agenda. One obvious question is can the Bank really implement legal reforms without addressing ‘political’ issues? Despite the Bank’s technocratic view of law, legal reform is by nature inherently political.<sup>38</sup> The danger is that by characterising legal reform as a technocratic process, the Bank will overlook contentious, qualitative issues in favour of less-contentious issues that are easy to quantify and measure.<sup>39</sup> Failing to confront the underlying political factors determining legal outcomes, and securing government commitment to the reform agenda, will clearly undermine the long-term sustainability of legal reform. Doing this, however, would inevitably put strain on the Bank’s mandate.

Related to this is the problem of who benefits from legal and judicial reform. The Bank has tended to place law on the side of markets rather than empowering individuals, in spite of its many claims about the advantages of legal reform for social development.<sup>40</sup> Law is viewed as means of protecting businesses, a buffer standing between economic growth and various political and social threats. As such, the Bank has mostly addressed issues relating to economic efficiency and property rights, rather than distributional considerations, questions of access to justice, the enforcing of political and civil rights, and the strengthening of criminal law (see case studies below).<sup>41</sup>

Meanwhile, the precise relationship between legal reform and economic development remains unclear. Little is known about the impact of the judicial system on economic performance, and critics argue that the Bank's justification of legal reform activity is based on spurious correlations between institutions and development. One analyst has argued that 'while history and comparative analysis support the view that a better judicial system fosters economic growth, there is no clear, empirical evidence showing the economic impact of a weak judicial system. The most that can be said at the moment is that the weight of opinion and evidence suggests the existence of some type of relationship.'<sup>42</sup>

This throws into doubt the claim that certain types of legal systems are best placed to promote economic development. Critics argue that the World Bank may be making the same mistake as the earlier law and development movement in trying to transplant 'neo-liberal legalism' in developing countries.<sup>43</sup> Possibilities of disagreement over the purpose and meaning of law, conflicts between different laws, and so forth, remain suppressed. What is lacking at present is a real discussion about whose rights are to be protected, to what extent, and to what effect.<sup>44</sup>

## **World Bank Legal and Judicial Reform Projects in Venezuela, Peru and Russia**

### *The Venezuela Judicial Infrastructure Project (1992)<sup>45</sup>*

This was the World Bank's first freestanding legal and judicial reform project. It had four basic components: (1) to strengthen the planning, budgeting, and management capacity of the judicial council; (2) To streamline courtroom administrative procedures; (3) to revitalise the judicial school; and (4) to rehabilitate existing and construct new courtroom facilities. The project was to be financed by \$30 million Bank loan and \$30million contribution by the Venezuelan government. The project quickly ran into problems and stalled for nearly two years. Several problems were identified at the evaluation stage: 1) lack of a comprehensive strategy; 2) no broad government commitment was obtained; 3) crucial structural impediments like judicial independence were not tackled; 4) the Bank's 'economic' focus was too narrow; 5) access-to-justice concerns were not addressed; and 6) there was no broad-based participation in the design and development of the project.

### *Peru Judicial Reform Project (1997)<sup>46</sup>*

The World Bank approved this project with a loan of \$22.5 million. The project was to focus on three areas: 1) administration of justice, 2) access to justice, and 3) judicial selection, training, and evaluation. However, the government's continued interference in the judicial branch prompted the Bank to postpone loan disbursements. The Bank formally terminated the Project in September 1998, before implementation had even begun. Two fundamental lessons emerged from the experience – first, that projects concerning structural changes such as judicial autonomy may prove to be more difficult to implement; and second, that government commitment is key to the reform process.

### *The Russian Legal Reform Project (1996)<sup>47</sup>*

This project is the largest legal reform project funded by the World Bank. It has four components—legislative drafting, legal information, legal education and judicial reform—and is one of the most complex projects of its kind. The project is being implemented by a NGO, the Russian Foundation for Legal Reform (RFLR). An analysis of the project after two years revealed that although it suffered from fewer shortcomings than earlier reform efforts, there are several factors that could derail the process. There is worry that, as in the Venezuelan case, the project does not have full commitment from participants. Excessive bureaucratic procedures have slowed down the process of reform. The narrow and apolitical nature of the Bank's legal and technical assistance sacrifices needed reforms in civil and human rights and criminal law. A full and final analysis of Bank performance can only be made after completion, and it is likely that the capacity and willingness of the government will play a pivotal role.

### 3.2 Corruption and the World Bank

There is general consensus among policymakers and academics that corruption is detrimental for development, and most multilateral and bilateral donors have introduced anti-corruption policies. After much initial reluctance, the Bank became the self-declared champion of the cause. In 1996, the Bank's President pledged that the World Bank would commit itself to fighting 'the cancer of corruption',<sup>48</sup> and Bank members have since published numerous background papers on the issue. In 1999, Wolfensohn claimed that 'As far as our institution is concerned, there is nothing more important than the issue of corruption.'<sup>49</sup>

The Bank defines corruption as 'the abuse of public office for private gain' (even though corruption is not confined to the public sector alone).<sup>50</sup> It is widely believed that 'malfunctioning government institutions constitute a severe obstacle to investment, entrepreneurship and innovation', raising the costs of development.<sup>51</sup> Most importantly, it is argued that bribery 'undermines the state's legitimacy' as regulator and protector of the market.<sup>52</sup> Bribery diverts potential foreign direct investment and can lead to major distortions within the public sector and within the economy as a whole.

The Bank, then, holds that the main cause of corruption is the unbounded discretion of public officials. It claims that the costs of rent-seeking (that is, behaviour which improves the welfare of someone at the expense of the welfare of someone else) are exacerbated by the lack of political will in many developing countries to combat the problem.

As a result, the Bank has called for more public accountability. The 1997 World Development Report highlights ways of reducing corruption, including: contracting-out services to private companies (possibly foreign firms with no close ties to the country); making rules more transparent; introducing market-based schemes that limit the discretion of regulators; and adopting administrative reforms that introduce competitive pressures into the government.<sup>53</sup> Another 1997 report, *Helping Countries Combat Corruption*, outlines the four 'pillars' of the Bank's anti-corruption strategy:<sup>54</sup>

(1) Minimising Fraud and corruption in Bank-supported projects. Within this context, the Bank has introduced a confidential hotline for reports on corruption, has tightened the procurement guidelines and has supported intensive audits of its projects. The aim is to become more 'client-oriented, with improved quality of services and portfolio'.<sup>55</sup>

(2) Helping countries that request assistance. Anti-corruption activities vary from strengthening legal systems, to anti-corruption dialogues, and also administrative and civil service reform.

(3) Mainstreaming corruption considerations in the Bank's operational work. Every Country Assistance Strategy (CAS) since 1999 should include an assessment of issues pertaining to governance and corruption.

(4) Supporting international efforts to fight corruption. The Bank has tried to further its partnerships with other multilateral donors in the fight against corruption, such as USAID, other development banks and the UNDP. It is a strong supporter of the OECD Anti-bribery Convention.<sup>56</sup>

### Uganda & Tanzania World Bank Anti-Corruption Initiative<sup>57</sup>

The key to the Bank's strategy in Uganda and Tanzania was making corruption a high-risk and low-return transaction, thus curbing its growth. The Bank emphasised that the purpose of reform was to change the system, not to lay blame on individuals. A series of workshops was held whereby various government, civil-society and legal representatives were brought together to discuss corruption. Another workshop was aimed at the media and enhancing capacity for investigative journalism.

Undoubtedly, these workshops are aimed at raising awareness regarding the importance of accountability in the public sector through strengthening institutional capacity and raising national integrity. However, at the evaluation stage the main finding was that although the process was helpful, participants felt that it was too focused on metropolitan areas and did not have far-reaching insight into dealings within rural communities. And despite its best intentions, the participatory approach does not have enough weight behind it to instigate government commitment. Beyond its role as facilitator, the World Bank does not have the ability to implement any recommended reforms.

Wary of overstepping its mandate, the Bank justifies its anti-corruption agenda on the basis that reducing corruption will remove impediments to growth. It is argued that corruption is linked to reduced foreign and domestic investment.<sup>58</sup> It distorts the private-versus-public expenditure relationship, diverting private investment and significantly increasing government expenditure. Moreover, in cases where government expenditure is skewed towards activities with rent-seeking rewards for officials, areas like health and education are likely to receive less funding.<sup>59</sup>

Despite these claims, there is still divergence among economists regarding the relationship between corruption and economic growth. Some have argued that bribes could actually induce economic growth by circumventing laborious bureaucratic red tape and hence increasing efficiency.<sup>60</sup> Others have likewise suggested that corruption can function as the 'much-needed grease in the squeaking wheels of a rigid administration'.<sup>61</sup> The Bank replies that even those who manage to avoid red tape are still heavily involved in inefficient time-management with a lot of effort being put into 'negotiating with public officials'.<sup>62</sup>

The debate on the relationship between corruption and economic growth was fuelled by controversies over East Asian development. In the 1980s and 1990s, East Asian states received large amounts of foreign investment despite high levels of corruption. Khan argues that in the face of this, the Bank's analysis looks naïve; it 'does not correspond to the reality of capitalist development in the past and contemporary developing countries in Asia. Any capitalist growth, particularly in its early "primitive accumulation" stage always gives rise to rents that are a precondition for growth ... while rents under certain conditions may concentrate resources necessary for growth, it may under other conditions create wasteful consumption or destructive forms of rent-competition'.<sup>63</sup>

Moving on to anti-corruption initiatives more specifically, to what extent can the Bank be effective in this area? As with legal reform, a fundamental problem is that the Bank has no real

enforcement mechanism or means of extracting commitment guarantees from governments, as the case studies above suggest. Even more importantly, the Bank's pro-business stance means that it has turned a blind eye to corrupt firms, especially powerful international businesses.<sup>64</sup> Despite the fact that corporations regularly bribe officials, vetting requirements are weak, and investigations only undertaken when the Bank is the main financier of a project (rather than one contributor).

Thus, although the government may be willing to enact a number of 'good governance' reforms, there can be strong internal and external forces that inhibit them from doing so.<sup>65</sup> Multinational companies are known to use bribes to achieve lucrative terms in privatization deals. In some circumstances, foreign companies persuade their own governments and aid providers to pressure developing country governments into accepting unfavourable contracts, using the withdrawal of aid as a threat. This was the case in Mozambique, when American officials allegedly pressured the Mozambican government to give a contract to a high-profile (and corrupt) international oil company.<sup>66</sup>

If the Bank fails to tackle the international aspects of corruption, then, only part of the problem will be addressed. As Nicholas Hildyard puts it, 'the problem of corruption is unlikely to be addressed by new regulations *unless* and *until* the well-documented structural and institutional barriers to their rigorous implementation are addressed.' This, according to Hildyard, requires an overhaul of the Bank's secretive culture, in order to make it more accountable, transparent, and open.<sup>67</sup>

A more fundamental problem is the argument that the Bank lacks the mandate to deal with corruption more directly, and does not have expertise in this area.<sup>68</sup> In the domestic context, its policies clearly extend far beyond state-market relations within developing states. For example, the Bank has explicitly called for greater accountability in government transactions, the reform of judicial systems, and better dialogue between parliaments and grass roots organisations.

As a result, the Bank is hemmed in by its neutral mandate. From a civil society perspective, anti-corruption initiatives usually revolve around calls for democratization, strengthening accountability, creating multi-party governments, and so on, but the Bank is forced to maintain that its initiatives could work in any state, democratic or authoritarian. This conflicts with the approach of some bilateral donors who see corruption as a threat to the legitimacy of democratic government, and with the Bank's own attempts to bring democracy issues into development (see below).

#### **4. Good governance as pro-market governance**

The goal of achieving the right conditions for market-led growth lies at the heart of the Bank's good governance strategy. Economic growth appears to be the ultimate end-point of the Bank's focus on institutions. 'Good governance' has generally been equated with 'sound development management'; the main thrust of the agenda has been directed towards public sector management, financial management, modernization of public administrative bodies, and privatization.<sup>69</sup> In this section, we look at three issues: macroeconomic policy, financial sector strengthening, and privatization.

## 4.1 Pro-market governance policies

### *Macroeconomic policy*

In the Bank's view, the private sector cannot flourish in the absence of sound macroeconomic policies, and there are three macroeconomic fundamentals.<sup>70</sup> First, developing countries should achieve and maintain macroeconomic stability. This is essential because factors such as high inflation can create uncertainty, reducing investment and leading to fluctuations in exchange rates. Second, developing countries should avoid price distortions, as these can discourage private investment and reduce efficiency. Third, developing countries should aim to liberalise trade and investment. The World Bank holds that open markets offer great opportunities for business, and increased access to resources, technology, and finance. Openness also creates competition, which stimulates the market, promotes efficiency, and forces developing country governments to follow policies that are consistent with international legal norms.<sup>71</sup>

The World Bank is involved in a number of projects that address these three areas of macroeconomic policy. In Senegal, for example, the Bank introduced a credit designed to improve the competitiveness of the economy by liberalising trade, facilitating trade and tax procedures, and supporting regulatory programs that promote competitive pricing of public utility inputs to the productive sector.<sup>72</sup> Another example is the Consolidation Structural Adjustment Project in the Kyrgyz Republic. The objective is to improve the country's fiscal and business environment, while attempting to ensure that acceptable levels of access and service are preserved for the poorest parts of society.<sup>73</sup>

Creating an enabling environment for business means more than simply getting the macroeconomic fundamentals right, however. Factors such as government credibility, mechanisms of public accountability, and private sector development are interlinked. Establishing trust is vital: if the public and potential investors don't trust the government, then its pro-market policies will have little impact. Hence, the government needs to focus on maintaining credibility, by means of legal and anti-corruption reforms. Recognising this, the World Bank produces a number of guidelines for fiscal and monetary policy, aimed at promoting stability and improving government credibility.<sup>74</sup>

### *Financial Sector Strengthening*

A sound financial sector is a fundamental component of any economy, as it provides financing and services to public and private actors alike. The 1997 World Development Report recognises this, laying stress on the need to safeguard financial systems by prudential regulation.<sup>75</sup> Banking systems are considered particularly important. In developing states, domestic banks are the primary form of financial intermediary: they are the largest recipients of public savings and the main source of capital for firms. Banking regulation is needed because—despite appearances to the contrary—banks are often extremely fragile due to insufficient capital, limited institutional capacity, risk taking, poor laws and ineffective supervision. Recommended supervisory measures include minimum capital requirements, restraints on insider trading, audit requirements, and increased transparency.<sup>76</sup>

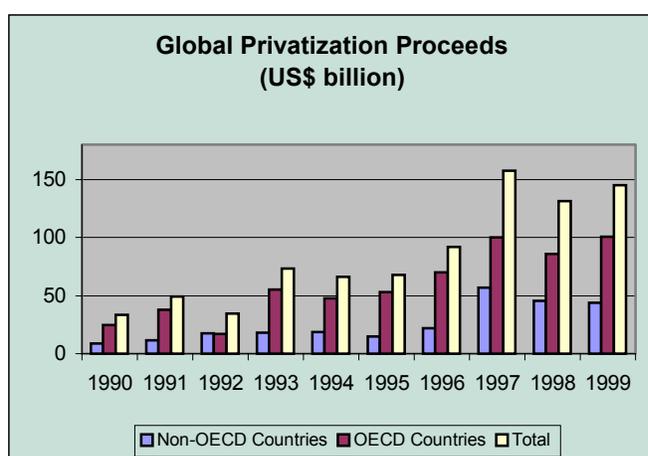
In practice, the World Bank Group's Financial Sector specialises in strengthening countries' financial systems by providing finance, policy research and advice, and technical support in key

areas.<sup>77</sup> The Banking Sector Restructuring and Privatization Project in Pakistan, for example, aims to achieve a competitive private banking system, a strong regulatory framework, and an effective banking court system.<sup>78</sup> The World Bank also has several projects that deal with different aspects of the financial system simultaneously, such as the Financial Sector Technical Assistance Loan Project in Brazil, which supports the development of institutional capacity to assist in the implementation of Brazil's financial sector reforms.<sup>79</sup>

### *Privatization*

According to the Bank, privatization leads to better governance and economic growth in developing countries. Neoclassical economic theory predicts that the transfer of state-owned entities to the private sector will promote ‘allocative efficiency’—defined as the net benefits flowing to and from the economy due to investments in an enterprise. On this view, privatization eliminates the problems associated with public enterprises—ambiguous objectives, inefficient incentive structures and lack of accountability mechanisms—which make them financial loss-makers, economically inefficient and socially irrelevant. Privatization stimulates better governance because it generates immediate revenues for governments that can then be invested, improving service provision and unlocking further opportunities for private sector development.<sup>80</sup>

In practice, the World Bank has undertaken a number of activities to promote private sector development.<sup>81</sup> It created the Private Sector Advisory Service—which now works in over one-hundred countries—to help build sound public policy.<sup>82</sup> It conducts research into improving understanding of the private sector in different regions,<sup>83</sup> and has set up an Investment Climate Unit to assess country investment conditions through surveys and indicators.<sup>84</sup> The Bank is also trying to encourage private sector participation in the provision of infrastructure.<sup>85</sup> All these efforts have helped to accelerate an increase in proceeds from privatization worldwide (see graph below).



Source: Mahboobi, ‘Recent Privatization Trends’ (OECD, 2000).

## **4.2 Issues arising from the pro-market good governance agenda**

It is clear that the privatization process depends upon the existence of strong institutions: namely, adherence to legal norms, high levels of trust, and low levels of corruption in a society. To be

successful, privatization must be undertaken in a transparent and well-regulated environment.<sup>86</sup> While the World Bank has consistently promoted privatization as a solution to governmental inefficiency and fiscal problems, it can nevertheless be damaging to developing countries if the preconditions are wrong.

This problem is symptomatic of the broader problems raised by trying to implement market and institutional reforms simultaneously. Introduced at the wrong time, liberalisation and macroeconomic reforms may actually weaken the regulatory capacity and accountability of the state, rather than strengthen it.<sup>87</sup> Deregulation can undermine the state's ability to control corruption by weakening its capacity to monitor private, public and corporate relations. An additional hurdle is that developing country governments trying to meet good governance conditionalities are forced to try and meet stricter demands for improved standards and economic performance, while trying to work with fewer resources and less influence.

Liberalization can also reduce political accountability. Accountability is a key aspect of any form of service provision; democratic governments should be accountable to their populations, and they risk being voted out if they are not. Private companies, however, are not formally accountable to their customers and in a non-competitive environment do not face the possibility of being ousted by other, more efficient providers. Where a monopoly exists and there are no formal accountability mechanisms, private companies can be more damaging than governments.<sup>88</sup>

Furthermore, in the case of privatization, the private sector is not always sufficiently developed. Private sector development is no easy task, and essential mechanisms must already exist within a country and within markets to support private growth and development. In the absence of these mechanisms, it is doubtful that privatising public enterprises will lead to the development of a large private sector.<sup>89</sup> For one thing, contracting-out to private firms for service provision is not always possible in developing countries where a well-developed private sector is not present. Contractors may not exist, and those that do may not be well-informed, efficient or productive. Thus, without a strong private sector, contracting-out public work can be damaging.<sup>90</sup>

There is also a contradiction between the Bank's pro-market stance and its focus on corruption in *public* institutions.<sup>91</sup> The 1997 World Development Report is full of references to the arbitrary and corrupt nature of the state, but as suggested above, the private sector can be corrupt as well. Although there is a clear need to prevent states from behaving in a corrupt manner and taking advantage of its citizens, there is little analysis to be found on the monopolistic powers of corporations, inter-firm bribery, capture, patronage and shady accounting practices in the private sector.<sup>92</sup>

Another problem is the relationship between the Bank's pro-market policies and poverty-reduction. For instance, how can privatization help the poor? According to the World Bank, privatization should reduce poverty through 'accelerated growth with improved distribution and by providing governments with fiscal space to focus on social spending'.<sup>93</sup> Poverty Reduction Strategy Papers (PRSPs) link poverty and privatization, suggesting a complementary relationship between the two.<sup>94</sup> However, a private sector company is unlikely to put human development and poverty at the top of its agenda; rather, private providers have a primary interest in making profits. This can exclude potential users, and when the service in question is essential for

development, the twin objectives of privatization and poverty reduction are at odds, according to many researchers.<sup>95</sup>

To give an example, in Nelspruit, South Africa, the 1998 sell-off of a water project to a British company, BiWater, led to increased complaints by residents. After privatization, residents reported having no access to water, having their water systems disconnected, not being able to afford the new tariffs, and receiving inflated bills based on meter readings. When residents complained to the local council, the council referred them to BiWater, which in turn informed residents that the meter-reading business had been outsourced to a separate company. This company then argued that it was not obliged to respond to complaints from the community.<sup>96</sup> Clearly, utility privatization did not help to alleviate poverty or increase accountability in this particular case.

Deregulation and privatization are thus not simple recipes for successful development because in many developing countries, the policy environment is not suitable for such policies. Their success depends on the ability of government to create a competitive enabling environment. This, then, takes us back to the tension identified in the introduction between good governance as a precondition for development and good governance as an objective of development. The Bank's policies vis-à-vis the private sector demonstrate that in the absence of certain pre-conditions, pro-market policies can have damaging as well as beneficial effects.

### **Privatization: A case study of the “loans-for-shares” scheme in Russia<sup>97</sup>**

The Russian experience during transition from a communist to a market economy in the 1990s is a good example of the challenges of privatization in the absence of a strong institutional environment. A ‘loans-for-shares’ system was adopted in 1995, by which the government allocated banking licences to private entrepreneurs. The newly formed banks were supposed to lend to private parties who could ‘buy’ the state enterprises. However, the newly created banks were licensed to print money and as such had the power to acquire government enterprises. The system was rife with corruption as licenses could be given out according to the government’s wishes.

Advocates of the system argued that although there was no guarantee that the new private owners would be competent managers, at least they could take advantage of the supposed ‘aftermarket’, making sure that the newly privatized businesses would end up in the hands of people who could best manage them in the long run. However, this assumption was never realised because of minimal demand due to a lack of private finance from which to begin an auction locally, as well as the increased unattractiveness of the businesses to international investors.

The net effect of the reform programme was that the state had less direct control over resources, and the financial benefits were siphoned off and not reinvested locally. Why did this happen?

- Privatization policies in Russia were inappropriate and inadequate. There was little understanding of the complexities of moving to a market economy.
- Certain entrepreneurial skills must exist for effective privatization, and these were limited in the former Soviet Union.
- Moving workers from low productive employment (under state employment) to unemployment (under privatization) is not an automatic improvement if no alternative opportunities for work are created.
- There must be a clear understanding of the distinction between ownership and control. If ownership of a company is through numerous, powerless shareholders but control is centralised through planners, they are not necessarily motivated to restructure their enterprises towards long-term growth if they are not also shareholders.

## 5. The state and Civil Society

State-civil society relations in recipient countries are a new area of interest for the World Bank. The Bank's recent willingness to address state-civil society relations is striking because previously, it dealt exclusively with developing country governments, excluding NGOs from the policy-making and policy-implementation process.<sup>98</sup>

Since the 1980s, the Bank (along with many other donor agencies) has undergone a process of transformation, putting increasing emphasis on partnership with civil society in formulating and implementing development projects. Terms such as 'civil society', 'Non-Governmental Organisation (NGO)', and 'participation' are now prominent in Bank discourse.<sup>99</sup> This section looks at three important aspects of state-civil society relations: those of participation, democratization, and decentralization.

### 5.1 Good Governance and Participation

The Bank defines participation as 'the process through which stakeholders influence and share control over development initiatives, and the decisions and resources that affect them.'<sup>100</sup> At the core of the participation agenda is the idea that those affected by development should form partnerships with aid organisations in order to define and implement policies. Terms such as 'stakeholder' and 'civil society' are used to refer to groups and organisations which act independently of the state and market in order to promote diverse interests in society.

The language of partnership and participation has two important aspects. First, the Bank is encouraging states to take the views of those previously excluded from the policy-making process into account: that is, the poor, the vulnerable, certain minorities, and so forth. A key assumption lying behind the participation agenda is that consulting civil society groups will make the development process more effective, as it will enable donors and governments to find out what the poor and minorities need.

One example of this working in practice is the 'report card' system developed in the Philippines, whereby citizens recorded their views on five pro-poor public services: health care, elementary education, water supply, housing, and the distribution of subsidised rice. The government used the findings to design new poverty alleviation strategies, and it has agreed to use report cards to track the performance of public agencies and allocate the government budget and public funds accordingly.<sup>101</sup>

Second, the Bank is extending the management and administration of development to actors within and the state: that is, Southern and transnational NGOs. The Bank views the rapid growth and expansion of NGOs in developing countries as evidence of the increasing demand for participation and genuine representation, and it values their abilities to transcend weak public sector capacity by providing services directly to the poor.<sup>102</sup>

### Key milestones in the World Bank discourse on participation

1989 *From Crisis to Sustainable Growth* recognises that ‘a strong civil society participating in public affairs’ is a crucial feature of good governance.<sup>103</sup>

1994 The World Bank publishes *The World Bank and Participation*.<sup>104</sup>

1999 The Bank unveils the *Comprehensive Development Framework* (CDF), a central component of which is the idea of partnership with stakeholders.<sup>105</sup> *Poverty Reduction Strategy Papers* (PRSPs) are founded on the idea of participatory development.<sup>106</sup>

2000-1 ‘Empowerment’ is chosen as an organising theme for the *World Development Report 2000-2001, Attacking Poverty*.

The Bank has consistently stressed the idea that the state should empower citizens by encouraging greater participation: ‘political regimes should honour the rule of law, allow the expression of political voice, and encourage the participation of poor people in political process.’<sup>107</sup> The Bank has urged states to be more responsive to the poor and establish social institutions for them. It has made progress in encouraging participatory development (for example, setting up forums and panels inviting civil society to discuss important issues and to monitor the Bank’s projects) and reaching out to groups previously excluded from the development process (for example, religious communities).

Despite these positive factors, however, critics have pointed to a significant gap between Bank rhetoric and reality. For some, the participation agenda is not radical enough. These critics argue that bringing NGOs into the development process is a cosmetic change, and that in reality the Bank remains wedded to top-down approaches, working with governments and other donors (rather than civil society) to address governance issues.<sup>108</sup> They also point to the fact that inter-NGO relations have their own hierarchies, with Northern and international NGOs wielding more influence at the Bank than local Southern NGOs.<sup>109</sup>

Furthermore, aside from the rhetoric, what has been crucially absent from the debate so far is a clear idea of *how* to involve civil society in development. Participation should mean more than merely being present at governmental meetings and conferences; real empowerment implies some input into policy-making. Attempts by the Bank and the IMF to make PRSPs participatory, for example, have been widely criticised by local and international NGOs for creating ‘talking-shops’.<sup>110</sup>

‘Real’ involvement in policy-making brings its own problems however, as mass consultation exercises are costly and time-consuming. Moreover, there is the thorny question of *who* should participate. On this question, the ‘stakeholder’ concept is particularly ambiguous. In theory, every member of a society has an interest in it, and is therefore a stakeholder. To what extent can NGOs, which are not elected, claim to represent society-wide interests? There is a potential conflict, for example, between contracting-out services to NGOs and supporting political processes. Formal democratic institutions such as parliaments might be undermined as a result.<sup>111</sup>

Finally, despite the hype, the amount of money being channelled through NGOs is still small compared with the millions of dollars flowing to governments, and NGOs have limited leverage over policy. Civil society organisations can apply to a small grants program, which provides on average only \$1000 to \$1500 per project, and supports a very limited range of activities.<sup>112</sup> A more common approach is for the Bank to lend directly to borrower governments that then sub-contract out to NGOs.<sup>113</sup> This is inefficient, however, as dependency upon government funding—which is often slow and erratic, and sometimes hostile to NGO agendas—significantly weakens NGO capacity to monitor the provision of government services.

## 5.2 Good Governance, democratization, and human rights

The World Bank's interest in democratization and issues such as civil liberties and human rights has increased since it adopted the good governance agenda. Indeed, the World Bank's interest in democratization is part of a broader trend towards promoting democracy by means of foreign aid, a long-term trend that became more pronounced after the end of the Cold War. Unlike bilateral donors, however, the World Bank's mandate prevents it from taking political issues into consideration when deciding whether to lend. As a result, the World Bank's approach to democratization has been technocratic—rather than overtly political—in character, focusing mainly on its economic and social aspects.<sup>114</sup>

In *The state in a Changing World*, the World Bank acknowledges the trend towards democratization in many developing countries, but refrains from embracing the concept because it is not able to 'establish a statistically convincing link between development performance and type of political regime'.<sup>115</sup> The report suggests that when citizens can express their opinions and participate in the policy-making, governments find it easier to implement reforms.<sup>116</sup>

Subsequent reports embrace democracy more emphatically. In *Attacking poverty* democracy is described as being 'intrinsically valuable for human well-being' and 'a good in itself'. It stresses the important role played by 'representative politics' in increasing transparency and accountability, and allowing the 'voices of the poor' to be heard.<sup>117</sup>

In addition, the Bank recently began to formulate a position on human rights and development. In 1998, the Bank accepted that property rights are fundamental to poverty reduction, and in May 2002, held a workshop to discuss the role of rights in development. The emergent human rights agenda is both an acknowledgement both of civil society pressure and academic research, such as that of Amartya Sen, which draws links between respect for civil and political rights and development. The Bank does not, as of yet, have a coherent position on human rights, but stresses that its role lies in the realization rather than the enforcement of rights.<sup>118</sup>

In practice, the Bank has brought the issue of democratic rights into its activities indirectly. One approach, for example, has been the promotion of participation as part of poverty reduction strategies. The strengthening of local government (see below) and participatory procedures in the community level is a 'trickle-up' strategy designed to enhance good 'democratic' governance and reduce poverty at the national level. Such policies are inherently constrained by the Bank's mandate, however. Some critics have argued that the Bank's tentative approach severely limits its ability to offer real change on issues such as democracy and human rights. Other critics

question the liberal-democratic models adopted by the Bank, arguing that it fails to explore the role of labour unions or socialist movements and pays inadequate attention to the issues of inequality.<sup>119</sup>

An alternative line of criticism identifies the dangers associated with the Bank's democracy agenda. According to one study, the World Bank's implicit acknowledgement of the political dimensions of good governance makes it vulnerable to political pressure from its major shareholders, especially the US Congress.<sup>120</sup> The study points to the contradiction between using conditionality, an 'undemocratic measure', to promote a governance agenda that 'clearly implies democratic processes—as underlined by the emphasis on accountability, transparency and participation'.<sup>121</sup> It is hard to see how external agencies, as the World Bank, can attempt to substitute for domestic political processes.

### 5.3 Good Governance and Decentralization

Decentralization—the transfer of authority and responsibility for public functions from the central government to intermediate and local government and/or the private sector—has been a feature of the development discourse for the last three decades. Administrative, fiscal, and market decentralization are concerned with public sector efficiency and the delivery of public services, whereas political decentralization (or devolution) refers to the broader transfer of governmental authority and responsibility.

The appeal of decentralization stems from its potential to improve state governance by means of increasing competition, accountability, and flexibility. As such, it is a 'cross-cutting' reform that has a bearing on most aspects of governance. The World Bank has been hesitant in adopting a clear pro-decentralization strategy, recognising that decentralization can either improve or undermine the state's capability. Decentralization can improve state effectiveness, but this is dependent on the quality of its design and implementation and on existing institutional capacities.

Evidence on the relationship between decentralization and improved governance is ambiguous. A number of World Bank studies have found a positive correlation between the two. One study used four dimensions of governance (citizen voice and exit; government orientation; social development and economic management) to demonstrate a statistically significant correlation between the degree of fiscal decentralization and good governance.<sup>122</sup> Recent World Bank research on decentralization also deals with the issue of corruption. One study concluded that fiscal decentralization in government expenditure is consistently associated with lower corruption.<sup>123</sup> However, evidence from other studies suggests that the link between decentralization and decreased corruption is not clear.<sup>124</sup>

Despite an initial reluctance to tackle the issue, the World Bank's formal stance on decentralization has gathered momentum over time. *The State in a Changing World* focuses on the need to 'bring the state closer to the people' by 'devolving power carefully'.<sup>125</sup> According to the report, decentralization improves accountability and incentives in the areas of local participation, service provision, and economic development.<sup>126</sup> The report is cautious in tone, stressing that any strategy of decentralization must begin with an assessment of the institutional

capability at the various levels of government. Where there is weak central government, the Bank suggests postponing decentralization or using a more carefully staged or sectoral approach in order to avoid potential pitfalls.<sup>127</sup>

In practice, a growing number of Bank funded projects are supporting sectoral decentralization strategies. Of the projects completed between 1993 and 1997, for instance, twelve per cent involved decentralising responsibilities to lower level of government, and the policy is further promoted via loans and country assistance strategies.<sup>128</sup> The World Bank is also funding several projects in co-operation with local governments, such as the Paraguay pilot community development project and the Provincial health project for Indonesia. The former, financed by a \$9 million loan from the IBRD, aims to support local communities in implementing poverty alleviation and community development activities; the latter, costing \$79 million, aims to bring about effective health sector decentralization in two Indonesian provinces.<sup>129</sup>

The approach of *Attacking Poverty* is proactive, seeing good local governance as instrumental to empowerment of the poor.<sup>130</sup> It argues that if decentralization is to be successful in enhancing the empowerment of the more marginalised groups, then effective mechanisms for popular participation and citizen monitoring of the local governments need to be put in place. Local government plays a core role in institutionalising participation, which in turn is supposed to increase the 'ownership' and sustainability of local development and contribute to poverty reduction. In theory, citizens' proximity to government makes the latter more vulnerable to public pressure, thus making it easier for citizens to become more informed and more demanding.<sup>131</sup> The report sets the goal of promoting inclusive decentralization and community development through the 'creation of powerful coalitions between more egalitarian social organisation at the community level and better local administration'.<sup>132</sup>

How, exactly, these coalitions are to be achieved remains vague, however, and the effect of *existing* power relations at the local level is not addressed sufficiently. Critics maintain that the strategy is too limited. As suggested in the section on democracy above, the World Bank avoids the issue of *democratic* decentralization, even though democracy is implied by the use of terms such as participation and empowerment.<sup>133</sup> Some studies have argued that the Bank's agenda lacks ambition, particularly for decentralization in African countries;<sup>134</sup> others point out that there has been too little decentralization because local governments fail to become truly representative or democratic.<sup>135</sup> One influential study argues that really effective decentralization requires a three-way working dynamic between central government, local government, and civil society.<sup>136</sup>

The same study points to the paradox of decentralization: the fact that decentralization demands 'more centralisation and more sophisticated political skills at the national level.'<sup>137</sup> In other words, the decentralization agenda cannot be divorced from other aspects of good governance: increasing voice, accountability, democracy, respect for the rule of law, and so on. Recent research emphasises the fact that to bring real benefits to communities, decentralization must take place in an accountable and representative way, and that devolved powers and rights must be enshrined in law. As one study puts it, 'pluralism without representative favours the most organised and powerful groups. It favours elite capture.'<sup>138</sup>

## 6. Conclusion

Over the last decade or so, promoting good governance has become one of the World Bank's central stated concerns and areas of focus. This report has outlined the content and development of the good governance paradigm and the Bank's vision of the ideal balance between state, market and civil society. Central to this is the notion that the state and institutions can and do play important roles in regulating and promoting the market.

Undoubtedly, the good governance agenda has a number of positive aspects. The fact that institutions have become a central focus of development debate makes room for a range of views on development. Importantly, the 2002 *World Development Report* makes it clear that 'one size does not fit all'; institutions need to develop in tune with a state's particular conditions and culture, and it is better to build on existing strengths rather than attempt to import alien structures and concepts.

Moreover, the good governance agenda marks an acknowledgement that markets cannot work in a vacuum, and that economic growth requires a good institutional architecture as well as sound macroeconomic fundamentals. As such, the 'post-Washington consensus' has a more balanced perspective than its predecessor. There is also increased recognition within the Bank that civil society can play a role in the development process, although exactly how this is realizable is unclear.

To a certain extent, the good governance agenda recognises that development cannot be tackled in the absence of tackling political institutions and culture. Some criticise the Bank, however, on the grounds that it has not gone far enough in this respect. The fact that the Bank remains restrained by its mandate on political matters leaves its definition of good governance biased towards the economic and technical aspects of governance, and against social or distributional matters. The political aspects of good governance are being tackled, but not directly or equitably.

As Santiso puts it, 'The World Bank's understanding of good governance continues to reflect a concern over the effectiveness of the state rather than the equity of the economic system and the legitimacy of the power structure.'<sup>139</sup> Much of the content of the good governance agenda, as described above, is concerned with a very narrow set of issues and interests: state accountability for business, less so for citizens; strengthening of property rights, but not land redistribution or attention to criminal justice issues. It is not surprising, then, that many critics ask, 'where are the poor?' in the Bank's governance agenda.

Hence, the Bank finds itself in a paradoxical position: the good governance agenda provides a vehicle for involvement in the political affairs of member states, while at the same time, its Charter expressly forbids it from doing so. When the Bank has ventured into political areas, it has rationalised its involvement on economic grounds. The paradoxes of the good governance agenda thus add weight to calls for a more fundamental re-evaluation of the Bank's role. Should it amend its charter so as to justify involvement in political matters? Alternatively, should the Bank revert to an earlier incarnation, that of a project-lending bank?

In a sense, the very fact that the good governance agenda exists in its present form is testament to the fact that civil society pressure can make a difference. Civil society organisations have

lobbied hard to make the Bretton Woods institutions more accountable, and encouraged them to address corruption and human rights concerns in their lending strategies. Although many factors influence the direction of Bank policy, NGOs and other civil society groups can make an important difference; the question is how far should they encourage the Bank to extend its mandate even further?

In response to this problem, some assert that the Bank should push further, and embrace justice and human rights concerns. The argument is clear: the Bank cannot tackle the issue of bad governance without tackling its political roots, which often lie in unaccountable and authoritarian domestic political systems. Democracy and development are interrelated issues. On this view, the Bank should extend its use of conditionality to encompass issues such as respect for human rights and democracy, and boycott projects which have a detrimental impact on political and civil rights or social justice.

Extending the mandate further might have negative, as well as positive, consequences. One important issue is the legitimacy of Bank involvement in issues of political governance. There is a striking division between developing and industrialised countries' enthusiasm for the good governance agenda. While the latter see it as an opportunity to make aid more effective and extend certain norms and practices to emerging market economies, developing-country governments see the good governance agenda as an intrusion and an attempt to justify slumping aid levels.

Good governance requirements risk appearing intrusive while the Bank's conception of good governance remains wedded to particular concepts and ideologies. Increasing flexibility in the *types* of good governance welcomed by the Bank would reduce this problem somewhat. It would have the added benefit of increasing 'ownership', the notion that reforms should be drawn up and implemented by the country concerned, rather than external actors. A further option would be for the Bank to improve its own governance, by becoming more representative, democratic, and accountable.<sup>140</sup> This, indeed, would assist with the implementation of the good governance agenda elsewhere; as the example of corruption in international business shows, governance in developing countries cannot be tackled without paying attention to wider issues.

A further problem with extending the Bank's mandate, however, is that it might overload the Bank's agenda and undermine its core lending activities, while exposing the Bank to political pressure from Northern governments. Until recently, the Bank did not specialise in institution-building; and currently, it does not specialise in human rights issues. It is not obvious that the Bank can address the institutional and rights-based aspects of development without the impact of overstretch detracting from its core lending activities. Moreover, yet deeper involvement of NGOs in governance-related issues does not solve the problems of legitimacy and accountability that plague the Bank, and might simultaneously undermine existing formal political institutions, such as national parliaments.

Linked to this issue is the question of means: how can the Bank successfully encourage good governance policies in developing countries without adding to the burden of conditionality? There is clearly a tension between the 'ownership' agenda on the one hand, which stipulates that reforms will not be effective if countries are not 'in the driving seat', and the practice of intensifying good governance conditions on the other. The Bank must devise strategies for

improving governance and ownership without simply adding to the existing number of conditions.

In sum, the World Bank has undoubtedly played an important role in shaping the international development agenda. Since the 1950s, the Bank has undergone significant changes. It has emerged as the leading development institution, and its attempts to articulate the 'good governance' agenda further consolidates this position. The good governance agenda marks a positive step for the Bank in many ways, but at present, the agenda is a compromise between the Bank's apolitical mandate on the one hand and calls for greater political involvement on the other. Addressing these issues will call for a much deeper evaluation of the World Bank's role, philosophy, and governance within, than seen so far.

## ENDNOTES

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### 1. Introduction

<sup>1</sup> See <http://www.oecd.org> and <http://www.imf.org/external/np/leg/index.htm> for OECD and IMF perspectives on governance. For the UNDP's view of governance, see UNDP, *Promoting Good Governance*.

<sup>2</sup> On the good governance agenda, see the Special Issue of *The Journal of Development Studies* on 'Changing the conditions for development aid.'

<sup>3</sup> See <http://www.worldbank.org>.

<sup>4</sup> World Bank, *Sub-Saharan Africa: From Crisis to Sustainable Growth*.

<sup>5</sup> Shihata, *Judicial Reform in Developing Countries and the Role of the World Bank*.

<sup>6</sup> Girishanker quoted in Santiso, 'Governance Conditionality and the Reform of Multilateral Development Finance', pp.14-15.

<sup>7</sup> The World Bank web site has colour-coded maps, graphs, charts and diagrams which capture the elements of good governance and institutional quality. See [www.worldbank.org/wbi/governance/datasets.htm](http://www.worldbank.org/wbi/governance/datasets.htm).

<sup>8</sup> See the two *Governance Matters* papers by Kaufmann, Kraay and Zoido-Lobadón published in 1999 and 2002. The papers focus on six dimensions of governance for 175 countries. A full list of contributing organisations and data sets can be downloaded from [www.worldbank.org/wbi/governance/pdf/govmatters2.pdf](http://www.worldbank.org/wbi/governance/pdf/govmatters2.pdf)

<sup>9</sup> *Governance Matters II*, p.3

<sup>10</sup> Mauro, 'Corruption and Growth'.

<sup>11</sup> Ibid.

<sup>12</sup> Hermes and Lensink, 'Changing the conditions for development: Aid', pp.1-17.

<sup>13</sup> Source: World Bank Operations Policy and Country Services, *Adjustment Lending Retrospective: Final Report*, 15 June 2001.

<sup>14</sup> See Kapur and Webb, 'Governance related conditionalities of the IFIs', pp.1-20; and Operations Evaluation Department, 'Adjustment lending in Sub-Saharan Africa: An update'.

<sup>15</sup> See Santiso, 'Governance conditionality and the reform of multilateral development finance: The role of the Group of Eight', p.4.

<sup>16</sup> On debates about selectivity in aid, see World Bank Policy Research Report, *Assessing Aid: What Works, What Doesn't and Why*; Kapur and Webb, 'Governance related conditionalities of the IFIs'; and Hermes and Lensink, 'Changing the conditions for development: Aid'.

### 2. Good governance and institutions

<sup>17</sup> Quoted in Miller-Adams, *The World Bank: New Agendas in a Changing World*, p.100.

<sup>18</sup> Santiso, 'Governance conditionality and the reform of multilateral development finance', p.9.

<sup>19</sup> Easterley, *The Elusive Quest for Growth*, p. 103.

<sup>20</sup> Stiglitz, *Whither Reform: Ten Years of Transition*, p.3.

<sup>21</sup> Wolfensohn, 'A proposal for a CDF'.

<sup>22</sup> Santiso, 'Governance conditionality and the reform of multilateral development finance'.

<sup>23</sup> *World Development Report 1997: The State in a Changing World*, p.1.

<sup>24</sup> Burki and Perry quoted in Santiso, Governance Conditionality, p.25.

<sup>25</sup> For this argument, see *World Development Report 2002: Building Institutions for Markets*, in general.

<sup>26</sup> Source: *Building Institutions for Markets*, p.2.

<sup>27</sup> *Building Institutions for Markets*, p.2.

<sup>28</sup> *Building Institutions for Markets*, p.3.

<sup>29</sup> *Building Institutions for Markets*.

### 3. Promoting sound public institutions: legal reform and anti-corruption measures

<sup>30</sup> See Kraay, Kaufman and Lobaton, 'Governance Matters' I.

<sup>31</sup> See Shihata, 'Legal Framework for Development: The World Bank's role in legal and judicial reform'.

<sup>32</sup> Richard Messick 'Judicial Reform and Economic Development', pp. 117-36

<sup>33</sup> Carothers, 'The Rule of Law Revival'.

- <sup>34</sup> See the World Bank web site, <http://www4.worldbank.org/legal/leglr/legalreform.html>.
- <sup>35</sup> World Bank, *The State in a Changing World*, p.100.
- <sup>36</sup> Shihata, 'Judicial reform in developing countries and the role of the World Bank.'
- <sup>37</sup> See Shihata, 'Initiatives in Legal and Judicial Reform' and World Bank, 'Annual Report 2001'.
- <sup>38</sup> Cranenburgh, 'Increasing State Capacity: What role for the World Bank?'
- <sup>39</sup> See the points made by Thomas Carothers in *Aiding Democracy Abroad*.
- <sup>40</sup> Rittich, 'Who's afraid of the critique of adjudication?'
- <sup>41</sup> Ibid., p.938.
- <sup>42</sup> Richard Messick 'Judicial Reform and Economic Development.'
- <sup>43</sup> Weaver, 'The discourse of law and economic development in the World Bank'.
- <sup>44</sup> Rittich, 'Who's afraid of the critique of adjudication?', p.941.
- <sup>45</sup> See *Halfway to Reform - The World Bank and The Venezuelan Justice System*.
- <sup>46</sup> See *Building On Quicksand: The Collapse Of The World Bank's Judicial Reform Project In Peru*.
- <sup>47</sup> See Weaver, 'In Neglect of the Political: Institutional Change, the World Bank and Russian Legal Reform'.
- <sup>48</sup> World Bank, 'Helping Countries Combat Corruption – Progress at the World Bank since 1997'.
- <sup>49</sup> See poverty references in James D. Wolfensohn's speech at the 9<sup>th</sup> International Anti-Corruption Conference, Durban, [www.worldbank.org/wbi/gac/durban.html](http://www.worldbank.org/wbi/gac/durban.html), October 1999.
- <sup>50</sup> Ofosu-Amaah, Soopramanien, Uprety, and Kishor, 'Combating Corruption: A Comparative Review of Selected Legal Aspects of State Practice and Major International Initiatives'.
- <sup>51</sup> Mauro, 'Corruption and Growth'.
- <sup>52</sup> World Bank, 'Corruption and Development', PREM Notes.
- <sup>53</sup> World Bank, *The State in a Changing World*.
- <sup>54</sup> World Bank, 'Helping Countries Combat Corruption – Progress at the World Bank since 1997'.
- <sup>55</sup> Ibid.
- <sup>56</sup> See <http://www.oecd.org/EN/home/0,,EN-home-31-nodirectorate-no-no--31,00.html>.
- <sup>57</sup> Leeuw, Van Gils, Kreft, 'Evaluating Anti-Corruption Initiatives: Underlying Logic and Mid-Term Impact of a World Bank Program'.
- <sup>58</sup> Wei, 'Corruption in Economic Development: Beneficial Grease, Minor Annoyance, or Major Obstacle?'
- <sup>59</sup> See James D. Wolfensohn's speech at the 9<sup>th</sup> International Anti-Corruption Conference, Durban, [www.worldbank.org/wbi/gac/durban.html](http://www.worldbank.org/wbi/gac/durban.html), October 1999 and Wei, 'Corruption in Economic Development'.
- <sup>60</sup> See Khan & Jomo, *Rents, Rent-Seeking and Economic Development*.
- <sup>61</sup> Bardhan, 'Corruption and Development: A review of the Issues', pp.1320-1346.
- <sup>62</sup> Wei, 'Corruption in Economic Development', p.13.
- <sup>63</sup> See comments in Andvig, Fjeldstad and Shrivastava, *A Report from the Workshop on Corruption: Critical Assessments of Contemporary Research*, Oslo 19-20 October 2000, NORAD, [www.norad.no](http://www.norad.no), November 2000.
- <sup>64</sup> Nicholas Hildyard, 'The Lesotho Highlands Water Development Project: What Went Wrong?'
- <sup>65</sup> Hildyard and Wilks, 'An Effective State? But for Whom?', p.53.
- <sup>66</sup> Bayliss and Hall, 'Privatization of Water and Energy in Africa', p.20.
- <sup>67</sup> Hildyard, 'The Lesotho Highlands Water Development Project'.
- <sup>68</sup> Marquette, 'Corruption, Democracy and the World Bank'.

#### 4. Good governance as pro-market governance

- <sup>69</sup> Santiso, 'Governance conditionality and the reform of multilateral development finance'.
- <sup>70</sup> *The State in a Changing World*, p.46.
- <sup>71</sup> *The State in a Changing World*, p. 48
- <sup>72</sup> See the World Bank web site <http://www4.worldbank.org/sprojects/Results.asp>.
- <sup>73</sup> For details of the project in the Kyrgyz Republic, see <http://www4.worldbank.org/sprojects/Results.asp>.
- <sup>74</sup> *The State in a Changing World*, p.50.
- <sup>75</sup> *The State in a Changing World*, p.65.
- <sup>76</sup> See *The State in a Changing World*, p.67. For an example of a banking-system improvement project in Pakistan, see <http://www4.worldbank.org/sprojects/Results.asp?st=DetSrc&Sec=FX>
- <sup>77</sup> See the World Bank Website, <http://www1.worldbank.org/finance/>
- <sup>78</sup> See <http://www4.worldbank.org/sprojects/Results.asp?st=DetSrc&Sec=FX>.
- <sup>79</sup> See <http://www4.worldbank.org/sprojects/Results.asp?st=DetSrc&Sec=FX>

- <sup>80</sup> *The State in a Changing World*, p.61.
- <sup>81</sup> One example is the Private Sector Development Project in Madagascar. This is expected to improve access, reliability, and affordability of key utilities, including transport. See World Bank Website; <http://www4.worldbank.org/sprojects/Results.asp?st=DetSrc&Sec=DX>
- <sup>82</sup> World Bank Website; <http://www.worldbank.org/privatesector/whatwedo.htm>
- <sup>83</sup> World Bank Website; <http://www.worldbank.org/privatesector/cg/index.htm>
- <sup>84</sup> World Bank Website; <http://www.worldbank.org/privatesector/ic/index.htm>
- <sup>85</sup> World Bank Website; <http://www.worldbank.org/privatesector/ppi/index.htm>
- <sup>86</sup> See *The State in a Changing World*, p.66; and Galal et al, *Welfare Consequences of Selling Public Enterprises*.
- <sup>87</sup> Sfetzel, 'Misunderstanding African Politics', p.233
- <sup>88</sup> Brett, 'Participation and Accountability in Development Management', p.1.
- <sup>89</sup> Bayliss, 'The World Bank and Privatization: a flawed development tool', p.5.
- <sup>90</sup> Marinussen, 'The Bank, the State and Development', p.72.
- <sup>91</sup> Della Porta, *Democracy and Corruption in Europe*, p. 177.
- <sup>92</sup> Hildyard and Wilks, 'An Effective State? But for Whom?', p.52.
- <sup>93</sup> [www.worldbank.org/html/fpd/privatesector/index.html](http://www.worldbank.org/html/fpd/privatesector/index.html)
- <sup>94</sup> See <http://www.worldbank.org/poverty/strategies/index.htm>.
- <sup>95</sup> Bayliss, 'The World Bank and Privatization', p.6..
- <sup>96</sup> <http://www.cosatu.org.za/shop/shop1002/shops1002-10.htm>
- <sup>97</sup> Stiglitz, 'Wither reform? The Years of the Transition'. [www.worldbank.org/research/abcde/stiglitz.html](http://www.worldbank.org/research/abcde/stiglitz.html)

## 5. The state and civil society

- <sup>98</sup> The Bank's Articles of Agreement specify that it lend only to developing country governments.
- <sup>99</sup> World Bank, *World Development Report 2000/2001: Attacking Poverty; and World Bank, Working Together: World Bank's Partnership with Civil Society*.
- <sup>100</sup> See the Bank's 1990 Participatory Development Learning Group (PDLG) report.
- <sup>101</sup> See <http://www.worldbank.org/eapsocial/asesocial/FilipinoReportCard.pdf>.
- <sup>102</sup> World Bank, *The State in a Changing World*.
- <sup>103</sup> World Bank, *From Crisis to Sustainable Growth*.
- <sup>104</sup> World Bank Learning Group on Participatory Development, *The World Bank and Participation*.
- <sup>105</sup> CDF brochure, available online, <http://www.worldbank.org/cdf/brochure.pdf>
- <sup>106</sup> See Wood/Bretton Woods Project, *The ABC of the PRSP*, April 2000. At <http://www.oneworld.net/cgi-bin/index.cgi?root=1410&url=http://www.brettonwoodsproject.org/topic/adjustment/index.html>.
- <sup>107</sup> See *Attacking Poverty*, p.99.
- <sup>108</sup> See <http://www.worldbank.org/html/extdr/gc/governance/governance.htm>
- <sup>109</sup> Hudock, *NGOs and Civil Society*.
- <sup>110</sup> See, for example, Abgure, *Still Sapping the Poor: A Critique of IMF Poverty Reduction Strategies at* <http://www.globalexchange.org/wbimf/imf0600.html>.
- <sup>111</sup> For example, see the arguments about PRSPs in Eurodad, *Many Dollars, Any Change?*
- <sup>112</sup> The guidelines for this program are available online, <http://www.worldbank.bg/Smallgrant2002/guidelines.pdf>.
- <sup>113</sup> World Bank Operations Evaluation Department, 'Nongovernmental Organisation in World Bank-Supported Projects: A Review'.
- <sup>114</sup> Stevens and Gnanaselvam, 'The World Bank and Governance', pp.97-105.
- <sup>115</sup> See IDA, 'Governance- the critical factor' and ODI, 'Political liberalisation and economic reform in developing countries'.
- <sup>116</sup> World Bank, *The State in a Changing World*.
- <sup>117</sup> World Bank, *Attacking Poverty*.
- <sup>118</sup> See Bretton Woods Update no.29, July/August 2002, at <http://www.brettonwoodsproject.org/topic/social/s2901hr.html>.
- <sup>119</sup> Braathen, 'New Social Corporatism: a discursive-comparative perspective on the World Development Report 2000/01, 'Attacking Poverty'.
- <sup>120</sup> Kapur and Webb, 'Governance related conditionalities of the international financial institutions', pp.1-19
- <sup>121</sup> Ibid.
- <sup>122</sup> Huther and Shah, 'Applying a simple measure of good governance to the debate on fiscal decentralization'.

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<sup>123</sup> Fisman and Gatti, R, 'Decentralization and corruption: evidence across countries.'

<sup>124</sup> Golooba-Mutebi, 'Decentralization, Democracy and Development Administration in Uganda, 1986-1996: Limits to popular participation', Thesis for the degree of Doctor of Philosophy, London School of Economics, 1999

<sup>125</sup> World Bank, *The State in a Changing World*.

<sup>126</sup> Ibid.

<sup>127</sup> Ibid. These potential pitfalls are: rising inequality between regions, the risk of the local government being captured by local elites and macroeconomic instability.

<sup>128</sup> See Litvack and Bird, 'Rethinking decentralization in developing countries.'

<sup>129</sup> <http://www.worldbank.org/html/extdr/newprojects/>

<sup>130</sup> World Bank, *Attacking Poverty*.

<sup>131</sup> Tendler, *Good Government in the Tropics*, p.144.

<sup>132</sup> Ibid.

<sup>133</sup> Moore, 'Putting politics into poverty reduction? The WDR on empowerment'.

<sup>134</sup> On the World Bank's vision for decentralization in Africa, see World Bank, 'Can Africa claim the 21<sup>st</sup> century?', World Bank, 2000.

<sup>135</sup> Ribot, 'Democratic Decentralization of Natural Resources.'

<sup>136</sup> Tendler, *Good Government in the Tropics*.

<sup>137</sup> Rudolf Hommes cited in Tendler, *Good Government in the Tropics*.

<sup>138</sup> Ribot, 'Democratic Decentralization of Natural Resources', p.1.

## 6. Conclusion

<sup>139</sup> Santiso, 'Governance conditionality and the reform of multilateral development finance', p.11.

<sup>140</sup> See Woods, 'The challenge of good governance for the IMF and the World Bank themselves'.