# AUSTRALIA

AND THE

# INTERNATIONAL FINANCIAL INSTITUTIONS

# 2007-08

Annual Report to the Parliament

Under the *International Monetary Agreements Act 1947* and the *International Bank for Reconstruction and Development (General Capital Increase) Act 1989*

The Hon Wayne Swan MP, Treasurer

ISBN 978-0-642-74531-6



Printed by CanPrint Communications Pty Ltd

# Australia and the International Financial Institutions 2007-08

Section 10 of the *International Monetary Agreements Act 1947* provides that the Treasurer shall prepare and cause to be laid before each House of the Parliament, as soon as practicable after the end of each financial year, a report on the operations of the Act and of the operations, insofar as they relate to Australia, of the Articles of Agreement of the International Monetary Fund (IMF) and the International Bank for Reconstruction and Development (IBRD) during that financial year.

Section 7 of the *International Bank for Reconstruction and Development (General Capital Increase) Act 1989* provides that the Treasurer shall prepare and cause to be laid before each House of the Parliament, as soon as practicable after the end of each financial year, a report on the operations of the Act during that financial year.

This report aims to meet the requirements of both Acts for the financial year 2007-08.

The IMF and the World Bank Group (comprising the IBRD, the International Development Association, the International Finance Corporation, the Multilateral Investment Guarantee Agency and the International Centre for Settlement of Investment Disputes) publish annual reports that provide comprehensive reviews of the operations of these institutions. The IMF and World Bank also make information available on their websites: www.imf.org and www.worldbank.org.

I commend this report to the Parliament.

WAYNE SWAN
Treasurer

# Contents

# Acronyms and abbreviations

| | |
|---|---|
| ARPP | Annual Report on Portfolio Performance |
| ARDE | Annual Review of Development Effectiveness |
| AusAID | Australian Agency for International Development |
| CIF | Climate Investment Funds |
| DC | Development Committee |
| DTC | Developing and transition countries |
| FTP | Financial Transaction Plan |
| G-20 | Group of 20 |
| GFRP | Global Food Crisis Response Program |
| IBRD | International Bank for Reconstruction and Development |
| ICSID | International Centre for Settlement of Investment Disputes |
| IDA | International Development Association |
| IDA15 | 15th Replenishment of the International Development Association |
| IEG | Independent Evaluation Group |
| IFC | International Finance Corporation |
| IFIs | International Financial Institutions |
| IMF | International Monetary Fund |
| IMFC | International Monetary and Financial Committee |
| MDGs | Millennium Development Goals |
| MIGA | Multilateral Investment Guarantee Agency |
| NAB | New Arrangements to Borrow |
| PRGF | Poverty Reduction and Growth Facility |
| QAG | Quality Assurance Group |
| RBA | Reserve Bank of Australia |
| SDR | Special Drawing Right |
| SFDCC | Strategic Framework for Development and Climate Change |
| UNFCCC | United Nations Framework Convention on Climate Change |

# Preface

This report compiles information on Australia's dealings with the International Monetary Fund (IMF) and the World Bank[1] for the period 1 July 2007 to 30 June 2008. Prior to 2002-03, separate reports were compiled for Australia's dealings with each of these multilateral institutions.

The 2007-08 report is in three sections:

**Section 1** briefly reviews key policy developments at the two international financial institutions (IFIs) since the period formally covered by this report.

**Section 2** reports Australia's relations with the IMF as required under the *International Monetary Agreements Act 1947*. This section covers Australia's representation at the IMF, its June 2008 Article IV consultation and participation in IMF Institute courses, meetings and visits. Australia's financial transactions with the Fund, involving both Special Drawing Rights (the IMF's unit of currency) and Australian dollars, are covered in Part 2 of this section.

**Section 3** looks at Australia's interactions with the World Bank as required under the *International Monetary Agreements Act 1947* and the *International Bank for Reconstruction and Development (General Capital Increase) Act 1989*. This section reports on the World Bank's mandate and institutions, Australia's shareholdings and contributions, Australian representation and activities of the Bank during 2007-08.

## Other sources of information

Treasury releases information on its activities through many publications, press releases, speeches and reports, including the Annual Report. Copies of Treasury publications are available on line at www.treasury.gov.au.

The IFIs also make a wide range of information available on their websites, www.imf.org and www.worldbank.org, including information on their responses to the global financial crisis and communiqués from recent IMF and World Bank Spring and Annual Meetings.[2]

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1 Australia is a member of each of the IMF, World Bank, Asian Development Bank (ADB) and European Bank for Reconstruction and Development (EBRD). Information on each institution is provided in the Treasury Annual Report and is also available from the institutions themselves through their annual reports. There is no legislative requirement to provide a separate Annual Report to the Parliament on the ADB and EBRD.

2 IMF and World Bank communiqués are available on the IMF's website: http://www.imf.org/external/news/default.aspx?cm

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# Section 1: Key developments

As this report covers the 2007-08 financial year only, it is important to acknowledge the substantial developments that have occurred at both the IMF and World Bank since this time, particularly due to the impacts of the global financial crisis since September 2008. The IFIs have responded and continue to respond to the impacts of the global financial crisis on developing and emerging market economies.

During 2008-09, key events surrounding the crisis have had a significant impact on the IFIs, especially the IMF. Of note is the G-20 Leaders' and the International Monetary and Financial Committee's (IMFC) agreement to treble resources available to the IMF from US$250 billion to US$750 billion, and Australia's commitment to the New Arrangements to Borrow (NAB). These commitments will ensure that the IMF has the resources available to maintain stability and support recovery in the global economy. It will enable the Fund to continue to act promptly to make substantial resources available, under adequate safeguards, to its member countries with external financing needs. Further, the G-20 Leaders' and the IMFC supported a general allocation of Special Drawing Rights (SDRs) equivalent to US$250 billion to increase global liquidity.

The advent of the crisis created an impetus for strengthening of Fund surveillance (the introduction of a joint Fund-Financial Stability Board (FSB) Early Warning Exercise and increased financial sector focus) and reform of lending facilities — including the introduction of the precautionary Flexible Credit Line (FCL), increased access limits and streamlined conditionality.

Governance reform will be a focus of the Fund in the upcoming year, following commitments by G-20 Leaders to reform the governance of IFIs. The IMF is accelerating the timeframe for completion of its next general review of quotas to January 2011 (from January 2013), with further increases in quota shares of dynamic economies, particularly emerging market and developing economies, expected. The Manuel Committee on IMF Governance Reform reported in March 2009 to the IMF's Managing Director, and changes to governance structures will be considered by the IMF in upcoming discussions on the topic.

A number of key developments have also occurred at the World Bank during 2008-09, including the Bank's commitment to triple lending by the main arm of the Bank, the International Bank for Reconstruction and Development (IBRD), to US$100 billion over the next three years; fast tracking International Development Association (IDA) commitments; establishing new funds to assist countries to respond to climate change, high food and fuel prices and the financial crisis; and expanding the International Finance Corporation's (IFC) trade finance programs.

Australia pledged $150 million over three years to the World Bank-administered Climate Investment Funds in September 2008. This funding will support large-scale deployments of low-carbon technology in major emitting developing countries and help vulnerable countries adapt to climate change. The Bank also formally launched its Strategic Framework for Development and Climate Change in 2008-09. Australia also contributed $50 million to the World Bank's Food Price Crisis Response Core Multi-Donor Trust Fund during 2008-09 to assist vulnerable countries to cope with higher and more volatile food prices.

World Bank Governors agreed to a voice and participation reform package at the October 2008 Annual Meeting. This first phase of reforms includes an additional African chair at the Executive Board, voting share realignment through an increase in basic votes and measures to increase developing countries' voting power at IDA. Once these reforms are implemented (expected to occur in 2009-10), Australia's voting power is expected to decline to 1.49 per cent from 1.52 per cent.

Looking ahead to the 2009-10 financial year, the World Bank is committed to accelerating a second phase of voice and participation reforms, focused on shareholding realignment, with agreement to be reached by April 2010 and is considering the need to deploy additional resources and review the capital adequacy of the IBRD, IFC and IDA.

# Section 2: Australia's interactions with the International Monetary Fund

(as required under the *International Monetary Agreements Act 1947*)

## Part 1: Australia's relations with the International Monetary Fund

### Mandate

The International Monetary Fund (IMF) was conceived at the United Nations' Bretton Woods conference held in July 1944, where representatives of 45 countries agreed to establish institutions to govern international economic relations in the aftermath of the Second World War. The IMF came into formal existence in December 1945, when 29 members ratified its Articles of Agreement.

The IMF was established to promote growth and prosperity. The IMF's purpose (set out in Article I of its Articles of Agreement) is to promote international monetary cooperation; facilitate the expansion of trade contributing to employment growth; promote exchange rate stability to avoid competitive devaluation; assist in the establishment of a multilateral system of payments; and make resources available to members to reduce the costs of balance of payments adjustments.

The IMF achieves its mandate by: conducting surveillance over the economic policies of members, and providing policy advice to assist members in achieving key domestic objectives; providing technical assistance and training to members, enabling them to build the expertise required to implement sound economic policies; and providing temporary financing to members experiencing balance of payments difficulties to reduce the cost associated with significant economic adjustment.

Australia became a member of the IMF in 1947. The *International Monetary Agreements Act 1947* formalised Australia's IMF membership. The Act contains provisions, which have been updated through time, to enable Australia to meet any obligations that may arise by virtue of its IMF membership. A brief outline of these provisions, along with an indication of whether the provision was used during 2007-08, is included in Table 2.1.

**Table 2.1: Activation of *International Monetary Agreements Act 1947* provisions in 2007-08**

| Section of the Act | Description of the provision | Provision activated |
|---|---|---|
| **Section 5A** | The Treasurer may provide the RBA with a written direction to exchange Special Drawing Rights (SDR) or foreign currency on the Commonwealth's behalf. | There is a standing direction to the RBA to this effect. |
| **Section 6 — Authority to borrow** | Provides the Treasurer with the authority to borrow funds in order to meet obligations as members of the IMF, World Bank, and New Arrangements to Borrow (NAB). | The provision was not activated during 2007-08. |
| **Section 7 — Issue of securities** | Provides the Treasurer with the authority to settle obligations by issuing non-negotiable and non-interest bearing securities, should it be acceptable to the IMF and World Bank. | No new securities were issued to the IMF in 2007-08. However, in the past Australia has issued the IMF with non-negotiable and non-interest bearing securities to pay the Australian dollar component of Australia's quota subscription and to maintain the Australian dollar value of this component in SDR terms. |
| **Section 8 — Payment of charges** | Provides Australia with the authority to pay service and interest charges on any borrowing. | The provision was not used during 2007-08. |
| **Section 8A — Appropriation for purposes of SDR department** | Provides the Treasurer with the authority to pay any obligations that arise due to Australia's membership of the SDR department. | The provision was exercised during 2007-08 to pay the quarterly interest charges on Australia's SDR holdings and the annual assessment fee. |
| **Section 8B — Appropriation for the purposes of the New Arrangements to Borrow** | Provides the Treasurer with the authority to meet its obligations under the NAB. Australia's total commitment in 2007-08 under the NAB is SDR 801 million. | The provision was not used during 2007-08. |
| **Section 8C — Financial assistance by Australia in support of Fund programs** | Provides the Treasurer with the authority to enter into a loan or currency swap arrangement with a member who has received an IMF support package. | The provision was not used during 2007-08. |

## Australia's representation

### Board of Governors

The Board of Governors is the highest authority within the IMF and consists of one Governor and one Alternate Governor for each member country. The Treasurer, the Hon Wayne Swan MP, has been Australia's Governor of the IMF since

3 December 2007.[3] During 2007-08 the Alternate Governor was the Secretary to the Treasury, Dr Ken Henry AC.

Member countries cast votes as required throughout the year. The Australian Governor's votes on IMF resolutions during 2007-08 are noted in Table 2.2.

**Table 2.2: Australian Governor's votes on IMF resolutions 2007-08**

| Resolution Title | Adoption date | Australian Governor's vote |
|---|---|---|
| Direct Remuneration of Executive Directors and their Alternates | 1 August 2007 | Supported |
| Financial Statements, Report on Audit and Administrative and Capital Budgets | 3 August 2007 | Adopted by consensus |
| Vote for the Managing Director | 1 November 2007 | Australia voted for Dominique Strauss-Kahn |
| International Monetary Fund (IMF) — Thirteenth General Review of Quotas | 28 March 2008 | Supported |
| Reform of Quota and Voice in the International Monetary Fund | 28 April 2008 | Supported |
| Proposed Amendment of the Articles of Agreement of the International Monetary Fund to Expand the Investment Authority of the International Monetary Fund | 5 May 2008 | Supported |

## International Monetary and Financial Committee

The International Monetary and Financial Committee (IMFC) advises the Board of Governors on the functioning and performance of the international monetary and financial system. Its 24 members represent the full IMF membership under the same constituency arrangements as apply in the IMF Executive Board (see below). International institutions, including the World Bank, also participate as observers in its meetings.

The IMFC meets twice a year, usually in September or October in conjunction with the full Governors' Meeting (the 'Annual Meetings'), and in March or April (the 'Spring Meetings').

The 2007 Annual Meetings coincided with the caretaker period of the 2007 Federal election. Mr David Parker, Treasury Executive Director, represented Australia at the Annual Governors' Meeting held on 22 October 2007, and represented the constituency of which Australia is part at the IMFC meeting on 20 October 2007.

The Treasurer represented Australia and the constituency of which Australia is a member at the IMFC meeting held on 12 April 2008.

3 From 1 July 2007 to 2 December 2007, the former Treasurer, the Hon Peter Costello MP, held this role.

Senior officials (Deputies) representing IMFC members attend preparatory meetings prior to each IMFC meeting. No Deputies meeting was held prior to the 2007 Annual Meetings. The 31 March 2008 IMFC Deputies meeting was attended by Treasury Acting Executive Director, Mr Christopher Legg.

## Executive Board

The Executive Board conducts the day-to-day business of the IMF and determines matters of policy under the overall authority of the Board of Governors. Executive Directors are appointed or elected by member countries or groups of countries.

The Board consists of 24 Executive Directors. Eight countries have single-member constituencies and appoint or elect their own Executive Director: the United States, Japan, Germany, France, the United Kingdom, China, Saudi Arabia and the Russian Federation. The remaining Executive Directors represent multi-member constituencies. During 2007-08, the constituency of which Australia is a member (the Asia and the Pacific constituency) comprised: Australia, Kiribati, the Republic of Korea, Marshall Islands, Federated States of Micronesia, Mongolia, New Zealand, Palau, Papua New Guinea, Philippines, Samoa, Seychelles, Solomon Islands and Vanuatu.

In June 2008, Australia's constituency held 3.84 per cent of the voting power in the IMF, and Australia independently held 1.47 per cent.

Mr Richard Murray of Australia was the Executive Director for the constituency from 1 November 2006 until 31 October 2008. Dr Hi-Su Lee of Korea succeeded Mr Murray as Executive Director on 1 November 2008.

The Executive Director is supported by an Alternate Executive Director and a number of senior advisors/advisors from various countries represented in the constituency. While the Executive Director may speak on behalf of individual members of the constituency, in the event of a formal vote in the Executive Board, all votes of the constituency must be cast as a bloc.

The Treasury, with input from the Reserve Bank of Australia (RBA) and other agencies as appropriate, provides briefing to the Executive Director on key issues being discussed by the Board.

## Australia's Article IV consultation

In accordance with Article IV of its Articles of Agreement, the IMF conducts regular discussions with the authorities of member countries on economic policies and conditions.

Australia's 2008 Article IV consultation included a visit by IMF staff from 23 June to 2 July. During their visit they met with the Treasurer, senior Treasury officials, the Governor of the RBA and senior RBA officials. They also met with officials from other agencies in the Treasury portfolio including the Productivity Commission and the

Australian Prudential Regulation Authority, and representatives from the business community and unions.

The staff report on the consultation is available at www.imf.org.

### Visits

During the IMF/World Bank Spring Meetings in Washington in April 2008, the Treasurer met with the IMF Managing Director, Mr Dominique Strauss-Kahn, and the IMF First Deputy Managing Director, Dr John Lipsky.

During 2007-08, senior Treasury officials met with the IMF First Deputy Managing Director, Dr John Lipsky (August and October 2007) and the IMF Deputy Managing Director, Mr Murilo Portugal (October 2007).

## Part 2: Australia's shareholding in the International Monetary Fund and financial transactions

A member's shareholding in the IMF is determined by its allocated quota which broadly reflects its weight in the global economy. Australia's quota as at 30 June 2008 was SDR3,236 million. A member's voting power in IMF decisions is also largely determined by its quota, with one vote allocated for each SDR100,000 of quota. In addition, each IMF member has 250 basic votes. During 2007-08, Australia held 1.47 per cent of total IMF voting power.

### Australia's financial transactions with the International Monetary Fund

Australia's financial transactions with the IMF in 2007-08 comprised:

- payments of Special Drawing Rights (SDR) charges and an annual assessment fee for Australia's allocation of SDRs;
- receipts of interest on Australia's SDR holdings;
- receipts of remuneration for Australia's contribution to IMF reserves;
- a payment by the IMF to Australia to maintain the value of Australia's quota; and
- transfers and receipts to facilitate Australia's contribution to the IMF's financial transaction plan, reflecting the borrowing and repayments of other members.

These transactions are described in the following sections.

## Special Drawing Rights charges, interest and assessment fee

The SDR is an international reserve asset (akin to a currency), created by the IMF to supplement the existing official reserves of member countries. The SDR also serves as the unit of account of the IMF. Its value is based on a basket of key international currencies (the US dollar, euro, Japanese yen and pound sterling).

SDRs are allocated to member countries in proportion to their IMF quotas. Each member country may choose to hold more or fewer SDRs than its net cumulative allocation.

Australia's allocation of SDRs remained at SDR471 million throughout 2007-08 while its actual SDR holdings at 30 June 2008 were SDR117 million. Australia's SDR allocation is held by the RBA, having been sold to the Bank by the Commonwealth for Australian dollars.

The IMF levies charges on the SDRs that have been allocated to each member and pays interest on the SDRs that are held by each member. Charges and interest payments are accrued daily at the same rate of interest and paid quarterly. The rate of interest on SDR holdings is calculated weekly and is based on a weighted average of representative interest rates on short-term debt in the money markets of the SDR basket of currencies.

In 2007-08, the Australian Government paid charges of SDR17.2 million on net cumulative allocations, and the RBA received SDR4.5 million interest on its holdings (Table 2.3).

In addition, the IMF levies an annual assessment fee to cover the cost of operating the SDR department. The fee is determined according to participants' net cumulative SDR allocations. Australia's annual assessment fee for the IMF's financial year ending 30 April 2008 was SDR33,413 (A$56,594) (see Table 2.3).

## Remuneration

The IMF pays remuneration (in effect, interest) on a member's reserve position in the IMF, except for a small proportion that is provided to the IMF as an interest-free resource. The amount of a member's reserves held by the IMF can change frequently through the year. It increases when the IMF calls on the member to contribute some of its currency to lend to other members, and decreases when borrowing members make repayments to the IMF that are then returned to the member. These payments are usually estimated in advance in the IMF's financial transaction plan.

Remuneration is accrued daily and paid quarterly, and the rate of remuneration is equal to the SDR interest rate minus an adjustment for burden sharing. When receiving the remuneration, the Government instructs the RBA to exchange the SDR amounts for Australian dollars at the prevailing exchange rate. Australia received remuneration payments in 2007-08 totalling SDR2 million (Table 2.4).

The IMF's burden-sharing mechanism makes up for the loss of income from unpaid charges and is also used to accumulate resources in the Fund's Special Contingent Account. Resources collected from members under the burden-sharing mechanism are refundable to them as arrears cases are resolved, or as may be decided by the IMF. Thus, resources collected for unpaid charges are refunded when these charges are eventually settled.

## Maintenance of value of IMF quota

During 2007-08, Australia's quota remained at SDR3,236 million. Part of this is held in reserve by the IMF in SDRs (this part is relevant for remuneration purposes) and part is held in Australia — a combination of promissory notes and cash amounts held at the RBA — in Australian dollars.

The exchange rate for the transactions between the Australian dollar and SDR amounts changes frequently. Consequently, the SDR value of the part of Australia's IMF quota held in Australian dollars is subject to change. Under the IMF's Articles of Agreement, members are required to maintain the value of their quota in terms of SDRs. The adjustment required to maintain the SDR value of the quota is called the maintenance of value adjustment, and is settled annually following the close of the IMF's financial year on 30 April.

During the IMF's financial year from 1 May 2007 to 30 April 2008, the value of the Australian dollar in terms of the SDR appreciated by 5.3 per cent. This meant that fewer Australian dollars were required to meet Australia's obligation to maintain the value of its quota in terms of SDRs. As the maintenance of value adjustment, the Australian Government received a payment of A$312.8 million from the Fund during 2007-08.

**Table 2.4: Australia's transactions with the IMF in 2007-08 (cash basis)[(a)]**

| | Amount in SDRs | Amount in A$ |
|---|---|---|
| **Interest on RBA SDR holdings** | | |
| For 3 months ending 31 July 2007 | 1,371,725 | 2,626,819 |
| For 3 months ending 31 October 2007 | 1,250,892 | 2,214,360 |
| For 3 months ending 31 January 2008 | 1,075,636 | 1,849,761 |
| For 3 months ending 30 April 2008 | 823,918 | 1,395,525 |
| Total interest received | 4,522,171 | 8,086,465 |
| **Charges on SDR allocation** | | |
| For 3 months ending 31 July 2007 | 5,054,427 | 9,679,102 |
| For 3 months ending 31 October 2007 | 4,715,507 | 8,347,508 |
| For 3 months ending 31 January 2008 | 4,151,654 | 7,139,560 |
| For 3 months ending 30 April 2008 | 3,251,390 | 5,507,097 |
| Total charges paid | 17,172,978 | 30,673,266 |
| **Annual assessment fee paid to SDR department** | 33,413 | 56,594 |
| **Remuneration for Australian holdings at the IMF** | | |
| For 3 months ending 31 July 2007 | 803,606 | 1,538,885 |
| For 3 months ending 31 October 2007 | 553,896 | 980,520 |
| For 3 months ending 31 January 2008 | 403,056 | 693,132 |
| For 3 months ending 30 April 2008 | 295,262 | 500,105 |
| Total remuneration received | 2,055,820 | 3,712,643 |
| **Maintenance of value transaction for 2007-08** | **n/a** | **312,875,201** |

(a) The totals may differ from the sum of the amounts shown due to rounding.

## Financial transactions plan and Australia's reserve position in the International Monetary Fund

The IMF manages its lending resources through a financial transactions plan (FTP). This is the mechanism through which the IMF selects the members whose currencies are to be used in IMF lending transactions and allocates the financing of those lending transactions among members included in the plan. Currencies of members included in the FTP can be used both for transfers (loans) from the IMF to borrowing members and for receipts (repayments) from borrowing members. Only currencies of IMF members with sufficiently strong balance of payments and reserve positions — such as Australia — are selected for use in the FTP.

In 2007-08, Australia was involved in both the transfer and receipts sides of the FTP. Australia conducted five transactions totalling A$87.2 million to facilitate transactions on the receipts side of the FTP and only one transaction, for A$74 million, on the transfer side. This reflected strong global economic growth at the time, with low levels of new IMF loan approvals and a number of borrowing members taking the opportunity to make early repayments.

Australian dollars can also be used by the IMF to settle minor $A-denominated administrative expenses incurred by the Fund. Australia did not transfer any additional funds to the IMF for this purpose in 2007-08. Australia receives ongoing interest on such transfers through the IMF's quarterly payment of remuneration.

As noted earlier, FTP transactions (and any transfers for administrative purposes) directly impact on Australia's reserve position at the IMF. With the value of receipts outweighing the value of transfers during 2007-08, the amount of Australia's reserves held by the IMF fell during the year, from SDR246 million to SDR239 million. This reserve position forms part of Australia's liquid international reserves because, subject to the representation of a balance of payments need, Australia can convert its SDR-denominated reserve asset into useable currency by drawing on the IMF.

Table 2.5 provides details of individual FTP transactions.

**Table 2.5 Australia's reserve position in the IMF 2007-08[(a)]**

| Date | Description | Debit (SDRs) | Debit (A$) | Credit (SDRs) | Credit (A$) |
|---|---|---|---|---|---|
| **Reserve position as at 30 June 2007** | | | | **246,034,045** | **438,954,585** |
| 2 Aug 2007 | FTP with Dominican Republic (Receipt) | 6,567,500 | 11,731,596 | | |
| 10 Aug 2007 | FTP with Turkey (Receipt) | 17,072,500 | 30,579,492 | | |
| 2 Nov 2007 | FTP with Turkey (Receipt) | 7,938,000 | 13,539,075 | | |
| 13 Mar 2008 | FTP with Turkey (Receipt) | 7,600,000 | 13,460,690 | | |
| 9 May 2008 | FTP with Turkey (Loan) | | | 43,000,000 | 74,001,029 |
| 11 Jun 2008 | FTP with Turkey (Receipt) | 10,450,000 | 17,870,151 | | |
| **Reserve position as at 30 June 2008** | | | | **239,406,045** | **409,399,264** |

(a) Because Australia's reserve position is denominated in SDRs and SDR/AUD exchange rates vary during the year, when expressed in Australian dollars, the 30 June 2008 reserve position does not exactly reflect summation of the opening position and transactions during the year.

# Part 3: Key activities of the International Monetary Fund

During 2007-08, the IMF made substantial progress in implementing its medium-term strategy with the key aims of: achieving a significant shift of quota and voting share to dynamic emerging market economies and enhancing the voice of low-income members in the Fund; securing a more reliable income base; and refocusing the Fund on its core mandate based on comparative advantage — accompanied by significant expenditure restraint, including down-sizing.

IMF Governors agreed on a second stage of quota and voice reform and a new income model in April 2008 and May 2008 respectively. Elements of these reforms require amendments to the IMF's Articles of Agreement, which must be accepted by three-fifths of members having 85 per cent of total voting power before they can come into effect. As of the end of the reporting period, treaty and legislative processes to enable Australia to accept the amendments were under way.

Other priorities in the IMF's medium-term strategy that were progressed in 2007-08 include: the strengthening of IMF surveillance; enhancing the Fund's role in emerging market economies; and engaging more effectively in low-income countries.

Further information on these reforms is provided below.

## Initial response to the financial market turmoil

By the end of 2007, there were growing concerns that the deterioration in financial markets in the United States could have systemic implications for global financial markets and the world economy.

In October 2007, the Financial Stability Forum (FSF, now the Financial Stability Board) was asked by the G-7 to analyse the underlying causes of the financial market turbulence and offer proposals. The Forum's report, together with a report prepared by the IMF on 'The Recent Financial Turmoil — Initial Assessment, Policy Lessons, and Implications for Fund Surveillance,' was considered by the IMFC at its meeting in April 2008.

The IMFC welcomed the FSF and IMF staff recommendations, emphasising the importance of international cooperation and the need to further strengthen the Fund's financial surveillance role and its capability to identify risks in the future.

During 2007-08, the IMF moved to strengthen its financial market expertise and early warning capabilities and to look more systematically at cross-country spill-overs and linkages between the financial sector and the real economy, better integrating this work into its overall surveillance activities.

Australia contributed to and strongly supported these developments through Ministerial involvement — in the IMFC and G-20, and bilaterally — and through our representatives at the IMF.

## Quota and voice reform

As outlined in the *Australia and the International Financial Institutions 2006-07* report, Australia has been a long-standing advocate of IMF quota and voice reform to address the under-representation of certain fast-growing nations — particularly in Asia — in IMF decision making. Australia's key objective has been to enhance the legitimacy and effectiveness of the IMF, including in its key role in crisis prevention and resolution, by ensuring that voting shares better reflect members' relative weight in the global economy.

The package of measures agreed by IMF Governors in April 2008 builds on the first stage of reform which provided ad hoc quota increases for the four most under-represented countries: China, Korea, Mexico and Turkey. The second stage included:

- a further rebalancing of quota shares for a broader range of members based on a new quota formula, with 54 countries receiving quota increases;
- a tripling of the number of basic votes which each country has, from 250 to 750, and protection of the share of basic votes in total IMF voting power into the future — this change increases the voting share of small and low-income IMF members relative to larger members; and
- provision for a second Alternate Executive Director in the IMF offices of large constituencies in recognition of their heavy workload — in practice this change will benefit the two African constituencies.

In terms of voting share, the main beneficiaries of the two stages of quota and voice reform are China, Korea, India, Brazil and Mexico. The largest declines in voting share are experienced by the United Kingdom, France, Saudi Arabia, Canada and Russia.

Australia's IMF voting share prior to the first stage of reform was 1.49 per cent. This share declined to 1.47 per cent following implementation of the first stage and will decline further to 1.31 per cent when the second stage becomes effective, reflecting quota increases received by other countries (while Australia's remains unchanged) and the increase in basic votes.

The decline in Australia's voting share is not expected to significantly alter the dynamic within our IMF constituency or our influence within the Fund. Australia has consistently argued that all members benefit from a more representative, legitimate and therefore more effective Fund.

## Surveillance

Effective IMF surveillance should enable the Fund to provide independent, objective and persuasive assessments and advice to policy makers at the national and international levels. The global financial crisis has highlighted the importance of the Fund's role in helping to identify key risks and vulnerabilities.

Consistent with the 2007 Decision on Bilateral Surveillance over Members' Policies, adopted by the Fund in June 2007, bilateral surveillance remains at the core of the Fund's work and an essential input into its multilateral and regional surveillance activities.

During 2007-08, the IMF worked to sharpen its analysis of the financial sector, macro-financial linkages, exchange rates, and cross-country spill-overs. In cooperation with other institutions, it deepened its work on identifying and addressing risks to financial stability. The Fund extended specific work on assessing vulnerabilities of emerging market economies to also include advanced economies. Steps were also taken to better integrate global and cross-country perspectives into bilateral surveillance.

Australia has continued to support and contribute to the IMF's surveillance reform agenda, emphasising the need to strengthen early warning capabilities and improve the responsiveness of members to Fund advice through candid Ministerial-level discussion of systemic risks and vulnerabilities.

## New income model

The IMF has traditionally relied on income from its lending activities to finance its general administrative expenses. There has been a rapid increase in IMF lending since late 2008 as a result of the global financial crisis. During 2007-08, however, IMF credit outstanding reached historically low levels, resulting in a substantial deficit in the Fund's administrative budget.

In response, the IMF implemented budget savings, primarily by refocusing the Fund on its core mandate and achieving significant staff reductions. The Fund also agreed on a new income model to diversify its income base and reduce reliance on lending as a source of income.

This new income model, agreed by IMF Governors in May 2008, is based on the recommendations of the Committee to Study the Sustainable Long-Term Financing of the IMF. The Committee's report was released in January 2007.[4]

Under this model, IMF income will be derived from: an investment endowment funded from the proceeds of the limited sale of IMF gold; an expanded investment authority to enhance returns; reimbursement of the direct costs incurred by the Fund in managing a donor-supported trust fund; and income from lending.

IMF gold sales will be conducted under stringent safeguards to ensure that any disruptions to the gold market are minimal. These safeguards include: strictly limiting sales to 403 tonnes, conducting them in an orderly and transparent manner and phased over perhaps three to four years; exploring the possibility of selling 'off-market' to official holders (resulting in only a re-distribution of official holdings); and conducting any on-market sales through the current Central Bank Gold Agreement (and any successor agreement) to ensure they do not add to the announced volume of sales from official sources.

The United States requires Congressional approval before it can support IMF gold sales in the IMF Executive Board.

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4 A copy of the Committee's report is available on the IMF website: http://www.imf.org/external/np/oth/2007/013107.pdf

Australia supported the changes on both the income and expenditure sides of the budget aimed at ensuring that IMF finances are placed on a sustainable long-term footing — thus promoting Fund effectiveness and reducing the risk of additional calls on members.

## Strengthening IMF corporate governance arrangements

Australia has been a strong advocate of IMF corporate governance reform to ensure the Fund can effectively respond to members, is accountable for delivering its mandate, and remains relevant and legitimate in light of changing economic realities.[5]

In 2007-08 the IMF began a comprehensive assessment of its governance arrangements which was prompted by the IMF Independent Evaluation Office (IEO) *Report on the Evaluation of Aspects of IMF Corporate Governance—Including the Role of the Executive Board,* released in May 2008.[6] The report considered issues such as: the respective roles and responsibilities of the Board of Governors, the IMFC, the Executive Board and Management; and Executive Board effectiveness. It concluded that 'reforms have not kept pace with changes in the environment in which [the Fund] operates' and that 'broader governance reform … holds the potential to strengthen the Fund's legitimacy, accountability, and effectiveness'.

The IMF Executive Board and Managing Director issued a Joint Statement on 27 May 2008 welcoming the report, and committing to a broader evaluation process that will examine the views of IMF members and external stakeholders.[7]

## International Working Group of Sovereign Wealth Funds

In 2007-08 the IMF facilitated the creation of an International Working Group (IWG) of Sovereign Wealth Funds (SWFs). The aim of the IWG was to help maintain the free flow of cross-border investment and open and stable financial systems by building trust with recipient countries and operating under sound commercially driven principles.

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5 See for example the Treasury working paper on the appointment processes for heads of the international financial institutions: http://www.treasury.gov.au/documents/1264/PDF/Tsy_Working_Paper%202007-04_IFI_appointments.pdf

6 A copy of the IEO report, along with background documents, is available on the IEO's website: http://www.ieo-imf.org/eval/complete/eval_05212008.html

7 A copy of the Joint Statement is available on the IMF's website: http://www.imf.org/external/np/sec/pr/2008/pr08121.htm

The IWG agreed to identify a common set of voluntary principles for SWFs.[8] During 2007-08, the IWG held its inaugural working session and formed a subgroup to undertake technical drafting work, chaired by Mr David Murray AO, Chairman of Australia's Future Fund.[9]

## IMF role in emerging market economies

The initial turmoil in global financial markets focused the IMF's role in emerging market economies on the macro-financial and cross-border risks for these countries. Work was undertaken in 2007-08 examining the temporary and structural trends in the global financial system affecting emerging markets, and how the Fund could improve its role in crisis prevention and resolution.

In September 2007, the IMF updated its vulnerability exercise for emerging market members to strengthen its analytical power and limit resource costs. The changes were aimed at ensuring that underlying vulnerabilities are not neglected in periods when the global environment is benign, crisis risks are low, and corrective policies can be more effectively adopted.

## IMF role in low-income countries

In 2007-08, the IMF produced a paper reviewing its role in low-income countries over the previous four years. While emphasising the Fund is not a development agency, the paper noted that its advisory, financing, and capacity building work — with a focus on macroeconomic and financial stability — is essential for low-income countries to be successful in achieving their development objectives, including poverty reduction. To support this role, the IMF Managing Director announced in February 2008 his intention to establish a low-income country unit within an existing IMF department.

A more comprehensive review, drawing together the various strands of the Fund's work in low-income countries, began in the second half of 2008. The aim is to enhance the focus and effectiveness of the Fund's engagement with these countries.

The sharp rises in the prices of food and fuel experienced in 2007-08 had a significant impact on many low-income countries, resulting in increased IMF financial support to eleven low-income countries during the year. The IMF also began a review of its Exogenous Shocks Facility (ESF) which provides financing to low-income countries affected by exogenous shocks such as rapid increases in food and fuel prices — with a

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8 The IWG comprised representatives from 25 IMF member countries: Australia, Azerbaijan, Bahrain, Botswana, Canada, Chile, China, Equatorial Guinea, Iran, Ireland, South Korea, Kuwait, Libya, Mexico, New Zealand, Norway, Qatar, Russia, Singapore, Timor-Leste, Trinidad & Tobago, the United Arab Emirates, the United States, and Vietnam. Saudi Arabia, the OECD and the World Bank participated as permanent observers.

9 In October 2008, the Santiago Principles for SWFs were presented to the IMFC and released publicly. The Santiago Principles are available on the IWG website: http://www.iwg-swf.org/pubs/eng/santiagoprinciples.pdf.

view to making the facility faster to access, easier to use, and capable of providing more financing. These changes were subsequently agreed.

Australia supports a strong role for the IMF, consistent with its mandate, in providing low-income countries with well-designed macroeconomic policy advice, financial support and technical assistance — in particular to promote macroeconomic and financial stability, address fluctuations in commodity prices, and help ensure debt sustainability.

During 2007-08, Australia continued to provide funding ($30 million over the 12 years to 2008-09) to the IMF's Poverty Reduction and Growth Facility trust account to support subsidisation of the interest rate on drawings by low-income countries under the Facility.

# Section 3: Australia's interactions with the World Bank

(This section of the report is required under the *International Monetary Agreements Act 1947* and the *International Bank for Reconstruction and Development (General Increase) Act 1989*.)

## Part 1: Australia's shareholding and relations with the World Bank

### Mandate

Established in 1944, the World Bank provides financial and technical assistance to developing countries around the world to achieve its mandate of poverty reduction and to promote sustainable development and inclusive growth. The World Bank's work focuses on achievement of the Millennium Development Goals (MDGs) and seeks to alleviate poverty in developing countries by concentrating on building the climate for investment, jobs and sustainable growth so that economies will grow; and by investing in and empowering poor people to participate in development.

### Institutions of the World Bank and Australia's shareholding

The World Bank consists of two main institutions — the International Bank for Reconstruction and Development (IBRD) and the International Development Association (IDA). The World Bank Group encompasses another three institutions: the International Finance Corporation (IFC), the Multilateral Investment Guarantee Agency (MIGA) and the International Centre for Settlement of Investment Disputes (ICSID). Each institution plays a different but collaborative role to advance the World Bank's vision of inclusive and sustainable globalisation.

#### International Bank for Reconstruction and Development

Established in 1944, the IBRD is a AAA-rated financial institution that aims to reduce poverty in middle-income and credit-worthy poorer countries by promoting sustainable development. The IBRD provides financing (loans, guarantees and related risk management products) and analytical and advisory services on a cost recovery basis. The IBRD has 185 member countries.

New lending commitments by IBRD rose in 2007-08 to US$13.5 billion for 99 operations. Development policy lending represented 29 per cent of total IBRD commitments, up slightly from 28 per cent in 2006-07. The East Asia and Pacific region received US$2.7 billion, representing 20 per cent of IBRD commitments.

In 2007-08, the IBRD's operating income increased to US$2.3 billion from US$1.7 billion in 2006-07. The IBRD obtains most of its funds by selling bonds in international capital markets. In 2007-08, medium- and long-term debt raised directly in financial markets by the IBRD amounted to US$19.3 billion (compared to US$10.7 billion in 2006-07). At the end of 2007-08, the IBRD's equity-to-loans ratio stood at 37.6 per cent, well above the target range of 23 to 27 per cent. Administrative expenses for the IBRD and IDA, budgeted at US$1.7 billion for 2007-08, are flat in real terms with a 2.9 per cent increase in nominal terms.

As at 30 June 2008, Australia held 24,464 shares in the IBRD, valued by the Bank at US$2.95 billion (A$3.07 billion),[10] representing 1.55 per cent of the total capital subscribed to by members and a voting power of 1.52 per cent. Of this amount, US$182 million (A$189 million) is paid in to the IBRD. The remaining US$2.77 billion (A$2.88 billion) is at call and would only be drawn down in the unlikely event that the IBRD is unable to meet its financial obligations. The World Bank has never drawn on Australia's uncalled capital subscriptions.

## International Development Association

Established in 1960, IDA focuses on the 82 poorest countries in the world, providing grants and highly concessional loans. The Association's resources help support country-led poverty reduction strategies in key policy areas, including: promoting economic growth; enhancing public sector governance and transparency; developing infrastructure; improving the quality of basic education; strengthening the fight against HIV/AIDS, avian flu and other communicable diseases; and building a healthy investment climate as a prerequisite for private sector investment. IDA has 167 members.

IDA is financed largely by contributions from donor governments, with replenishments of resources occurring every three years. Additional financing includes transfers from the IBRD's net income, grants from the IFC, and borrowers' repayments of earlier credits. Negotiations over the 15th Replenishment of IDA (IDA15) were concluded in December 2007, with donor countries pledging a record US$25.2 billion. In total, IDA15 will provide US$41.7 billion, an increase of US$9.5 billion over the 14th Replenishment of IDA (IDA14) and the largest expansion in donor funding in IDA's history. The IDA15 process also agreed a number of important policy outcomes including: further strengthening IDA's performance-based allocation system; improved aid effectiveness through accelerated decentralisation of staff and decision making authority to the field, particularly in fragile states; and an increased focus on the special needs of small states.

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10 The valuations in this report are sourced from the relevant institution's latest financial reports. Valuations are then converted to Australian dollar amounts using the exchange rate as at the reporting date. There will be differences between values reported by the World Bank and Australian-recorded values for budget purposes due to different accounting methodologies.

Australia is a longstanding supporter of IDA, making a financial contribution at each three-yearly replenishment since 1961. In December 2007, Australia agreed to contribute A$583 million to IDA15, increasing our burden share from 1.46 per cent for IDA14 to 1.80 per cent for IDA15. Australia's IDA contribution was enhanced through an additional A$107.9 million contribution in May 2008 for debt relief initiatives including the Heavily Indebted Poor Countries Initiative and the Multilateral Debt Relief Initiative, and for arrears clearance. During negotiations, Australia focused on ensuring improved responsiveness, particularly for fragile countries, and enhanced effectiveness.

During 2007-08, IDA commitments reached US$11.2 billion. This funding, including US$7.8 billion in credits and US$3.4 billion in grants, supported 199 operations. In 2007-08, countries with annual per capita income of up to US$1,065 were eligible for IDA assistance. The largest share of IDA resources was committed to Africa, which received US$5.7 billion, or around 50 per cent of total IDA commitments. South Asia received US$2.8 billion and East Asia and the Pacific received US$1.8 billion. Vietnam and India were the largest single recipients of IDA funding. IDA's operating income of US$1.8 billion was US$931 million higher than in 2006-07.

### International Finance Corporation

Established in 1956, the IFC promotes economic development through the private sector within the World Bank's overall poverty reduction mandate and is the largest provider of multilateral financing for the private sector in the developing world. The IFC invests with local or foreign business partners in developing economies, often in high-risk commercial environments, to add new commercial capacities in local markets and demonstrate viable opportunities to local business. The IFC also assists private businesses in developing countries to secure financing in international financial markets and provides advice and technical assistance to business and governments. The IFC has 179 member countries.

In 2007-08, new IFC investments totalled US$16.2 billion, an increase of 34 per cent from the previous year. The IFC committed US$11.4 billion from its own account and mobilised an additional US$4.8 billion from other sources. This funding supported 372 private sector investments in 85 developing countries. Projects in the poorest countries accounted for 45 per cent of 2007-08 investments. In terms of 2007-08 investments by region, Latin America and the Caribbean received the largest proportion (26 per cent), followed by Europe and Central Asia (24 per cent) and East Asia and the Pacific (14 per cent). In 2007-08, the IFC generated a net income of US$1.55 billion. The total administrative budget in 2007-08 will increase to US$656 million from US$598 million, an increase of 9.8 per cent.

As at 30 June 2008, Australia's shareholding in the IFC was 47,329 shares, valued by the IFC at US$47.3 million (A$49.2 million), representing 2.00 per cent of the IFC's total capital stock and a voting power of 1.97 per cent. All 47,329 shares are paid in.

## Multilateral Investment Guarantee Agency

Established in 1988, the Multilateral Investment Guarantee Agency (MIGA) promotes foreign investment into emerging economies by offering political risk insurance (guarantees) to investors and lenders. MIGA also provides technical assistance and advice to help developing countries to attract and retain foreign investment. Since 2005, MIGA has focused on four priority areas: investment in IDA countries; conflict-affected environments; complex infrastructure transactions; and south-south investments. MIGA has 172 members.

In 2007-08, MIGA issued 38 guarantees amounting to US$2.1 billion (a 53 per cent increase over 2006-07), representing the largest amount of new gross exposure in the institution's history. During 2007-08, MIGA had 23 new projects, three of which were in the Asia and the Pacific region. During 2007-08, MIGA's operating income was US$55 million, compared with US$49 million in 2006-07, and total gross revenues earned from guarantees amounted to US$38.9 million, compared to US$36.3 million in 2006-07. MIGA's total administrative budget for 2008-09 is US$38.2 million, which is a 2.7 per cent increase over the 2007-08 budget but represents no increase in real terms.

During 2007-08, MIGA continued to focus on its engagement in IDA countries with US$690 million going to 15 projects in IDA-eligible countries.

As at 30 June 2008, Australia held 3,019 shares in MIGA, valued by MIGA at US$32.7 million (A$33.9 million), representing 1.73 per cent of the total capital subscribed to by members of MIGA and a voting power of 1.50 per cent. Of this amount, US$6.2 million (A$6.44 million) is paid in to MIGA, with the remaining US$26.5 million (A$27.5 million) at call.

## International Centre for Settlement of Investment Disputes

Established in 1966, the International Centre for Settlement of Investment Disputes (ICSID) is an autonomous institution that helps encourage foreign investment by providing international facilities for conciliation and arbitration of investment disputes between foreign investors and their host countries. Australia signed the Convention on the Settlement of Investment Disputes Between States and Nationals of Other States on 24 March 1975, and deposited its instrument of ratification on 2 May 1991. ICSID has 144 member countries.

A record 48 proceedings were instituted in 2007-08, including the registration of 31 new requests for arbitration and one new request for conciliation, bringing the total number of cases registered since ICSID's establishment to 268.

Australia is a member of ICSID. Each member country is equally represented in ICSID and there is no system of shareholding.

### Australian development cooperation with the World Bank

The World Bank Group is Australia's largest non-government development partner. As a partner it has considerable comparative advantages that assist the Australian Government in realising its international development assistance objectives. These advantages include:

- substantial financial resources;
- significant convening power to bring together donors, partner governments and other multilateral and international financial institutions; and
- extensive knowledge resources and analytical capabilities.

In terms of development cooperation, the Australian Agency for International Development (AusAID) works with the World Bank through a range of joint activities to complement Australia's IDA contributions. Joint activities undertaken through co-financing agreements enable Australia to leverage the resources and global expertise of the World Bank in support of Australia's international development assistance objectives.

Joint activities include a variety of research and analytical projects and collaboration is at country, regional and thematic levels. In the Pacific, Australia is working with the World Bank in most countries and in a variety of thematic areas such as health, education, economic growth, climate change and water and sanitation. Australia also works with the World Bank at the regional level through programs such as the Pacific Region Infrastructure Facility which is being undertaken with two other important partners, the New Zealand Agency for International Development and the Asian Development Bank. Similarly, in East Asia, South Asia, the Middle East and Africa, Australia partners with the World Bank across a wide variety of single and multi-donor programs to further the Government's international development objectives.

In 2007-08, AusAID worked with the World Bank on 92 joint activities funded through co-financing agreements with a total value of $195 million in that year. These activities ranged from small research projects such as analysis on integrating small states into the world economy through to involvement in multi-donor programs like the $33 million contribution in 2007-08 to the Afghanistan Reconstruction Trust Fund.

## Australian representation at the World Bank

### Board of Governors

The highest decision-making body of the World Bank Group is the Board of Governors, which consists of one Governor from each member country. During 2007-08, Australia was represented by two Governors — the Treasurer, the Hon Wayne Swan MP, and prior to this, the former Treasurer, the Hon Peter Costello MP. Australia's Alternate Governor is currently the Parliamentary Secretary for

International Development Assistance, the Hon Bob McMullan MP. Prior to this, the former Parliamentary Secretary to the Minister for Foreign Affairs, the Hon Greg Hunt MP, held this position.

A list of resolutions on which Governors voted during 2007-08 is set out in Table 3.1 together with the Australian Governor's votes.

**Table 3.1: Australian Governor's votes on World Bank Group resolutions — 1 July 2007-30 June 2008**

| Resolution title | Adoption date | Australian Governor's vote |
|---|---|---|
| **IBRD** | | |
| Direct Remuneration of Executive Directors and their Alternates | 13 August 2007 | Supported |
| Financial Statements, Accountant's Report and Administrative Budget | 22 October 2007 | Supported |
| Allocation of Net Income | 22 October 2007 | Supported |
| Transfer from Surplus to Replenish the Trust Fund for Gaza and West Bank | 4 June 2008 | Supported |
| Transfer of IBRD Surplus to Food Price Crisis Response Trust Fund | 13 June 2008 | Supported |
| **IDA** | | |
| Membership of the Republic of Estonia | 30 July 2007 | Supported |
| Financial Statements, Accountant's Report and Administrative Budget | 22 October 2007 | Supported |
| Latvia — Change in Membership Status | 22 January 2008 | Supported |
| Membership of the Republic of Lithuania | 3 April 2008 | Supported |
| Additions to Resources: Fifteenth Replenishment | 23 April 2008 | Supported |
| **IFC** | | |
| Financial Statements, Accountant's Report and Administrative Budget | 22 October 2007 | Supported |
| Membership of the State of Qatar | 13 June 2008 | Supported |
| **MIGA** | | |
| Financial Statements, Accountant's Report and Administrative Budget | 22 October 2007 | Supported |

## Executive Director and constituency office

The World Bank's Executive Boards (IBRD, IDA, IFC and MIGA) take decisions on the day-to-day business of the World Bank Group and determine matters of policy under the overall authority of the Board of Governors. Each Board currently consists of 24 Executive Directors. Executive Directors elected to the IBRD Board are automatically elected to the IDA and IFC Boards. MIGA Executive Directors are elected separately, however in practice, MIGA has the same Executive Board (currently

MIGA's Board is identical to the IBRD's Board). An Executive Director is appointed by each of the five member countries that have the largest number of shares in the capital stock, currently the United States, Japan, Germany, the United Kingdom and France. The remaining Executive Directors are elected to represent either individual countries (for example, China and Saudi Arabia have single-country offices) or a constituency of countries.

Australia belongs to a constituency that also includes Cambodia, Kiribati, the Republic of Korea, Marshall Islands, Federated States of Micronesia, Mongolia, New Zealand, Palau, Papua New Guinea, Samoa, Solomon Islands and Vanuatu. As at 30 June 2008, Australia's constituency at the IBRD held 3.45 per cent of total voting power. As a result of the voice and participation package agreed in October 2008, our constituency's voting power is expected to increase to 3.55 per cent.

By agreement between constituency member countries, the staffing of Australia's constituency office rotates. Dr Jim Hagan from Australia currently serves as the Executive Director (IBRD, IDA, IFC and MIGA) for Australia's constituency. Dr Hagan is serving a four-year term as Executive Director, from 1 August 2007 to 31 July 2011. Prior to this, Mr Joong-Kyung Choi from Korea held the Executive Director position for two years ending 31 July 2007. Australia also holds an advisor position in the constituency office.

Mr Do-Hyeong Kim from Korea has held the Alternate Executive Director position for the constituency since 15 February 2008. Prior to this, Mr Choi served as Alternate Executive Director from 1 August 2007 to 14 February 2008. As per constituency arrangements, New Zealand will hold the Executive Director position for two years from 31 July 2011 and Australia will hold the Alternate Executive Director position during this period. The current constituency agreement ends in 2013. The constituency will need to negotiate a new staffing rotation arrangement prior to this time.

The briefing provided to the Executive Director on matters coming before the Executive Board is prepared by relevant Australian Government departments and agencies, principally Treasury and AusAID. Periodic consultations are also held with non-government organisations.

## Development Committee meetings

The Spring and Annual Meetings of the Development Committee, a joint ministerial committee of the World Bank and IMF, are normally held in April and October of each year, respectively. Australia was represented at the April 2008 meetings by the Treasurer, the Hon Wayne Swan MP, and the October 2007 meetings by the then Executive Director of Macroeconomic Group, Mr David Parker. Preparatory meetings of the Development Committee (Deputies) were attended in 2008 by Chief Advisor (International) of Macroeconomic Group, Mr Chris Legg and in 2007 by the then Executive Director of Macroeconomic Group, Mr Terry O'Brien.

### Visits

In August 2007, Treasury hosted a visit by World Bank President Robert Zoellick and arranged meetings between Mr Zoellick and Australian Government ministers and senior officials, including meetings between the Prime Minister Kevin Rudd and President Zoellick in Bali (December 2007) and Washington (April 2008).

During 2007-08, Treasury also hosted visits by Dr Graeme Wheeler, World Bank Managing Director (January 2008); and Mr Jim Adams, Vice President, East Asia and Pacific (November 2007 and February 2008).

# Part 2: Key activities of the World Bank

## Key developments

### Long-term strategic direction

In October 2007, World Bank President Zoellick announced the Bank's new long-term strategic direction, which is to be pursued in order to obtain the goal of inclusive and sustainable globalisation. The strategy is based on six pillars that aim to reposition the Bank to deal with changes in its client base as a result of changing global dynamics. The pillars are: overcoming poverty in the poorest countries; better engagement with middle-income countries; addressing the special challenges of fragile and conflict-affected states; actively addressing regional and global public goods (for example, climate change, HIV/AIDS); supporting development in the Arab world; and fostering a 'knowledge and learning' agenda across the Bank Group.

Australia broadly supported the new Bank Group strategy, particularly its focus on fragile states, during the World Bank's October 2007 Annual Meeting and April 2008 Spring Meeting, including in Australia's constituency statements at both meetings.

### Global food security

The World Bank continued to respond to major development challenges including global food security. Food and oil prices accelerated sharply in the first half of 2008, having a dramatic impact on poverty levels, especially in food importing developing countries. Australia welcomed the Bank's leadership on a rapid and coordinated response to rising global food and fuel prices. This included: setting out the 'New Deal for Global Food Policy' in April 2008 to catalyse global action across several areas, including trade, biofuels and investment; and coordinating its response with other multilateral development agencies, specifically the UN-led High Level Taskforce on the Global Food Security Crisis.

In May 2008, the Bank created its own Global Food Crisis Response Program (GFRP), which outlined its short-, medium- and long-term response to high food prices and included US$1.2 billion (including US$200 million in grants) in expedited financial support and technical advice to the most severely affected countries. In order to facilitate the involvement of a broad range of development partners to support the GFRP, the World Bank created a Multi-Donor Trust Fund (to which Australia contributed A$50 million in 2008-09). The GFRP is additional to other efforts by the World Bank Group to address the global food crisis including enhanced support for global agriculture.

### Climate change strategy

The Bank has significantly stepped up its work on climate change in view of its importance as a challenge to sustainable development and poverty reduction. In 2007-08, the Bank sought to clearly define its engagement in climate change through developing its Strategic Framework for Development and Climate Change (SFDCC). The Framework will help the World Bank Group to provide better support to developing countries in achieving their poverty reduction and growth objectives, while better recognising the added costs and risks of climate change, as well as new economic opportunities arising from global climate change policies.

A key new initiative supporting implementation of the Bank's climate change strategy is the World Bank-administered Climate Investment Funds (CIF), designed to assist developing countries to address urgent climate change challenges and to promote international cooperation on climate change. The CIF comprise two multilateral funds, the Clean Technology Fund, which finances large-scale approaches to the demonstration and deployment of low-carbon technologies in high-emitting developing countries; and the Strategic Climate Fund, which aims to scale up finance for innovative approaches to climate change adaptation and mitigation. The CIF will be an important source of additional financing for climate change to fill an immediate gap while a future climate change regime under the United Nations Framework Convention on Climate Change (UNFCCC) is agreed and established.

### Voice and participation reform

Voice and participation reform aims to improve the influence that developing countries and countries with economies in transition (DTCs) have over the governance, policies and decision making in multilateral institutions such as the World Bank and IMF. It follows from the 2002 Monterrey Consensus on Financing for Development. Voice reform encompasses structural and non-structural reforms. Structural measures include changes to shareholding, voting shares and voting majorities. Non structural measures relate to: broader effectiveness and governance (for example, Executive Board reform, merit-based selection); and responsiveness (such as decentralisation, enhanced communication with client countries). In 2007-08, World Bank management worked with the Executive Board and member countries to develop a suitable package of voice and participation reforms.

Australia is a strong proponent of reform of the IMF and World Bank and has played a constructive role in progressing discussions on reform options in many forums, including at the Executive Board, international meetings and bilateral discussions.

## Managing for development results

The World Bank supports the world's developing countries in their efforts to boost economic growth, lower poverty and improve the living conditions of people. The 'results agenda' adopted by the Bank aims to ensure that development assistance yields sustainable poverty reduction. The Bank attempts to evaluate its success by directly measuring the impacts of its products and services on poverty reduction. The primary measurement tool is results-based Country Assistance Strategies, specifying expected linkages between the Bank's interventions and long-term development goals, including measurable indicators of progress.

Additionally, the IDA Results Measurement System shows aggregated results across IDA countries. Linked to the MDGs framework, it reflects the priorities and processes of national poverty reduction strategies and assesses IDA's contribution to development results. It measures results on two levels: aggregate country outcomes; and IDA's contribution to country outcomes. An interactive website now facilitates the tracking of key indicators (www.worldbank.org/results).

## Operations evaluation

Evaluation of the World Bank's project quality is an integral part of the Bank's performance review processes. There are several major independent reviews of Bank performance prepared by the Independent Evaluation Group (IEG) and the Quality Assurance Group (QAG). The IEG is an independent unit within the Bank that reports directly to the Board of Executive Directors. The IEG's evaluations seek to provide an objective basis for assessing the results of the Bank's work, to ensure accountability in the achievement of objectives and to facilitate learning from experience. The QAG monitors the quality of World Bank operational work, including loans and advisory services, during implementation.

The *Annual Review of Development Effectiveness* (ARDE) is the flagship publication of the IEG. In 2007-08, the IEG found that overall development outcomes of Bank lending had improved over the medium term, albeit not over the past year. The IEG found a rising 'disconnect' between project supervision ratings and final project outcomes that could point to weak incentives for accurate project reporting. The IEG cautioned against over-optimism in assessing ongoing project performance, and called for vigilance to ensure that the drop in project performance in 2006-07 did not foreshadow a persistent decline.

The *Annual Report on Portfolio Performance* (ARPP) produced by QAG provides a strategic overview of the size, composition and quality of the Bank's lending portfolio and the Analytic and Advisory Activities program. Outcomes of the 2007-08 ARPP included:

- The Bank's portfolio at end 2007-08 consisted of 1,617 operations with net commitments of US$111.7 billion. The relative shares of the IBRD and IDA in the portfolio shifted over the previous five years, with IDA's share increasing from 39 per cent to 43 per cent. The portfolio was less concentrated compared to five years ago, with the share of the top 10 borrowers declining from 57 per cent to 50 per cent.

- The development outcomes of operations exiting the Bank's portfolio suffered a decline in 2006-07. The share of 2006-07 exits with satisfactory outcomes in terms of number of projects was 76 per cent, compared to 82 per cent the previous year. The declines are mainly traceable to lower performance in Africa (particularly in fragile states), and in three Sector Boards — Health, Nutrition and Population; Public Sector Governance; and Finance and Private Sector Development. The ARPP noted that addressing weaknesses in project design and ensuring adequate and timely restructuring of problem projects in these segments of the portfolio would help improve its performance.
- About 40 per cent of fragile states projects exiting were rated unsatisfactory. This is close to the average performance during the previous three years. However, the performance of fragile states projects in the Africa region was 49 per cent satisfactory in terms of number of projects, compared to 75 per cent for non-Africa region fragile states projects. This indicates that there is substantial scope for improvement in the performance of Africa region projects in fragile states.
- Several Sector Boards made significant strides in improving outcomes, notably Environment, Economic Policy, and Urban Development.

In 2007, the IEG evaluated the development effects of IFC projects implemented in 1996-2006, and this year it reviewed development effects for 2005-2007. In 2007, 71 per cent of selected samples were satisfactory in terms of development benchmarks and standards, while 63 per cent of evaluated projects in the previous ten years achieved satisfactory outcomes. The IEG evaluation showed that 85 per cent of projects had a strong correlation between development results and profitability. However, development results have been weaker in smaller projects, particularly in projects of less than US$5 million.