The Inter-American Development Bank

In October 1985, the Inter-American Development Bank (IDB) completed its first twenty-five years of operations. The IDB, which currently lends about $3 billion each year to member countries in Latin America and the Caribbean, is owned by 43 countries from both within and outside the region. Its cumulative lending now stands at over $30 billion, which has financed more than 1,500 development projects with a total investment of over $100 billion. This article[1] describes the structure and operations of the IDB and the evolution of its role since the emergence of international debt problems in 1982. It also discusses the future role of the IDB.

The origins of the IDB

Towards the end of the last century, the countries of Latin America began to express a strong interest in a regional financing agency. At the first International American Conference held in Washington DC in 1889 and 1890, a resolution was passed calling for the establishment of an inter-American bank. But this initiative, along with several others in the early years of this century, was not acted upon. In 1944, however, the principles agreed at Bretton Woods to help solve the problems of underdevelopment gave a fresh impetus to calls for a Latin American development bank. These calls were renewed at the meeting of the Pan-American Union (later the Organisation of American States) in Mexico in 1945. Nevertheless, it was not until the setting up of an inter-American development bank was proposed by President Kubitschek of Brazil in 1958, and supported by President Eisenhower of the United States, that sufficient momentum was given to the idea. Shortly afterwards, a special committee of the Organisation of American States was created to draft the Articles of Agreement of the proposed Inter-American Development Bank. That Agreement came into effect in December 1959 when ratified by virtually every country in Latin America, plus Haiti and the United States. The IDB, whose headquarters are in Washington, officially began operations in October 1960; its first loan—$3.9 million for improving the water and sewerage systems of Arequipa, Peru—was approved in February 1961.

Purpose and functions

The purpose and functions of the IDB are set out in Article I of the Articles of Agreement. Given the importance of Bretton Woods as the source of much of the inspiration for the IDB, there are many similarities between the goals defined for it and those laid down in the Articles of the International Bank for Reconstruction and Development (the World Bank).[2] The main purpose of the IDB is to 'contribute to the acceleration of the process of economic and social development of the regional developing member countries'. The functions of the IDB are defined as 'utilising its own capital, funds raised in financial markets, and other available resources, for financing the development of the member countries'. It is also charged with encouraging private investment in activities contributing to economic development and with helping member countries achieve 'a better utilisation of their resources, in a manner consistent with the objectives of making their economies more complementary and of fostering the orderly growth of their foreign trade'; and with providing 'technical assistance for the preparation, financing, and implementation of development plans and projects'.

Ownership

The IDB is owned by its member countries, whose subscription to its capital (which is partly paid in) determines each member's voting power in the Board of Governors and the Board of Executive Directors. Since its creation, the IDB has more than doubled its membership from twenty countries to forty-three. In the late 1960s several newly-independent Caribbean countries joined. However, the main increase came in the 1970s when, in an effort to attract additional resources, the Articles of Agreement were amended to allow developed countries other than the United States to join. Like the United States, these countries are not eligible to borrow from the IDB. However, they do benefit from the opportunities for the procurement of goods and services under IDB loans.[3] The first to join was Canada, in 1972. Since then, sixteen countries from outside the region have joined. They comprise most countries in Western Europe (including the United Kingdom), Israel, Japan and Yugoslavia.

Voting and control

The basic authority of the IDB is vested in the Board of Governors. Each member country elects one Governor, usually a Minister of Finance or central bank Governor. The Board of Governors meets at least once a year to

(1) Prepared by Paul Luke of the Bank of England's International Division.
(2) The financial structure and operations of the World Bank are described in an article in the March 1985 *Bulletin*, page 47.
(3) In 1984, 44% of convertible currency disbursed by the IDB under loan agreements was used to purchase goods and services from member countries outside Latin America and the Caribbean.

review the IDB's operations and make major policy decisions. The Board of Governors appoints a Board of Executive Directors to supervise the operations of the IDB within the framework of the general guidelines set by the Governors. The Executive Directors—who meet weekly—decide the institution's operational policies, approve loan and technical co-operation proposals, set interest rates, authorise borrowings and approve the administrative budget. The Board currently comprises twelve Executive Directors: eight for Latin America and the Caribbean; one each for Canada and the United States; and two representing non-regional members. Decisions relating to the IDB's capital—including loans therefrom—are by simple majority, while decisions relating to the IDB's soft loan window—the Fund for Special Operations—are by two-thirds majority. In spite of the growth in the number of 'non-borrowing' members, the bulk (54%) of the IDB's capital—and hence voting power—is supplied by the 'borrowing members', while the United States accounts for 34.5%, Canada 4.5% and the non-regional members 7%. The United Kingdom is the joint second largest non-regional subscriber after Japan and contributes 1% of the IDB's capital.

Resources

The IDB relies on several sources of funds to finance its activities. The cumulative growth of resources and lending is shown in Table A.

Table A
Cumulative resources and loans authorised, 1961–84
$ millions; *percentages in italics*

	Resources	Loans	Loans as percentage of resources
1961	1,353	294	*21.7*
1964	2,038	1,166	*57.2*
1968	5,176	2,798	*54.1*
1972	8,999	5,441	*60.5*
1976	14,386	10,222	*71.1*
1980	23,989	17,840	*74.5*
1984	34,022	27,772	*81.6*

Capital subscriptions

The capital of the IDB is currently divided between the 'ordinary' capital, which was created when the IDB was set up, and the 'inter-regional' capital, which was created to house capital subscriptions of the non-regional members that joined in the 1970s. It is intended to merge the capital in the near future. At the end of 1984, the IDB had total subscribed capital of $24.5 billion, with a further $10 billion committed for 1985 and 1986 under the Sixth General Increase of Resources. Of the $24.5 billion total, $2.2 billion was paid in, while the remainder was callable. The balance between callable and paid-in elements has altered over the years. When the IDB was established in 1960 with total capital of $1 billion, its paid-in capital constituted 47% of the total (with callable capital representing 53%). Since then, in the course of the various increases in IDB resources that have taken place, the paid-in share has declined steadily. Thus the Sixth General Increase in 1983—which covered the period 1983 to 1986 inclusive—added $15 billion to the IDB's authorised capital, of which only 4½% was paid in.(1) (A corollary of this decline in paid-in capital is the increasing reliance of the IDB on the world's financial markets in the form of borrowing against callable capital—see below.) At the end of 1984, the United Kingdom's share of subscribed capital was $243.3 million, of which $21.6 million was paid in.(2)

Borrowing on capital markets

The IDB's callable capital, which has never involved money outlays by the subscribing member governments, enables the IDB to tap private savings and to channel them to high-priority development projects in Latin America and the Caribbean. Borrowings, which take the form of bond and note offerings, as well as syndicated loans, are not allowed to exceed the callable element of the capital subscriptions of the non-borrowing members of the IDB. The IDB's bonds are traded in all the world's major financial centres: United States rating agencies allocate them the highest possible rating (AAA) and the IDB has an equally high standing in other capital markets. Borrowings provide the bulk of the IDB's resources for lending. In 1984, the IDB made twenty-two individual borrowings on the world capital markets for a total of $1.8 billion, the largest amount in its history. The new issues brought outstanding borrowings as of end-1984 to $6.1 billion. Of the $1.8 billion raised in 1984, nearly a third was in US dollars. Geographically, about 67% was raised in non-regional markets, of which £160 million, including a £60 million eurosterling issue, was borrowed in the United Kingdom. The weighted average effective interest rate on the outstanding principal of borrowings, after deducting discount, was 9.2%.

The Fund for Special Operations

The Fund for Special Operations (FSO) is separate from the IDB's capital resources. It was created as a concessional facility to make long-term, low-interest loans for projects otherwise outside the scope of normal international financing (eg social development projects). By the end of 1984, the FSO's resources reached $8 billion: these resources are derived from direct, fully-paid contributions by member governments. At the end of 1984, the United Kingdom's share of the FSO was $151.9 million, 1.8% of the total value of the FSO.

Other funds

From its earliest years, the IDB has been given responsibility for administering special funds provided by various countries for regional development. These funds totalled $1.2 billion by end-1984, the two largest being the $525 million Social Progress Trust Fund—financed

(1) The paid-in element of World Bank capital increases has also fallen over the years, from 20% in 1946 to 8¾% under the latest increase; similar reductions have taken place in regional development banks in other parts of the world (eg the Asian and African Development Banks).

(2) The United Kingdom's paid-in subscriptions have been made in sterling. However, the capital of the IDB is expressed in terms of 'United States dollars of the weight and fineness in effect on January 1, 1959'. Each member country is therefore required to 'maintain the value' of its currency held in the capital (except for currency derived from borrowings) against the US dollar at 1 January 1959. Under the Sixth General Increase, all paid-in contributions are required to be made in the member country's own currency, which must be made freely convertible.

by the United States—and the $500 million Venezuelan Trust Fund. These two funds specialise respectively in social development loans and finance for regional economic co-operation.

Complementary financing

The complementary financing programme was created in 1976. Complementary finance involves the granting by the IDB of two loans: the first, chargeable to its own resources; and the second, 'complementary', loan, suitable for funding by commercial banks. Participations in the complementary loan are then sold, without recourse to the IDB, to the financial institutions submitting the most competitive offers. Conditions in the last two years have not been propitious for such operations, but the IDB succeeded in arranging a $52 million complementary loan early in 1985 for the Jaguas hydroelectric project in Colombia. This brought the cumulative total of complementary loans since 1976 to around $700 million. Since complementary loans are legally IDB loans, the borrower generally gets more favourable terms and conditions than if the funds were obtained independently. The participating bank for its part benefits from the IDB's analysis and supervision of the project being financed and also from the IDB's record of borrowers' compliance with their obligations.

Reserves

Net income from the capital resources of the IDB and from the FSO is allocated to 'general reserves' in order to provide for possible future losses on loans or any annual excess of expenses over income. Smaller 'special reserves' are also maintained against capital resources to meet the IDB's obligations created by borrowing or by guaranteeing loans. The bulk of reserves is held in the form of debt issued by member governments. At the end of 1984, the ratio of capital reserves to outstanding lending from the capital was 31%; the ratio in the FSO was 10%.

Lending

In Article III of the Articles of Agreement of the IDB, it is stated that 'loans made or guaranteed by the Bank shall be principally for financing specific projects'. Therefore the IDB has operated primarily as a provider of project finance, although some lending which has not been strictly related to projects has also taken place. To help carry out these functions, the IDB has a network of field offices extending to every one of its borrowing member countries.

Lending terms and conditions

The terms and conditions of IDB loans—which are made both in local currencies and in the currencies of non-borrowing members—depend on the resources used. The foreign exchange portion of loans from capital resources is currently amortised over periods between ten and twenty-five years, including grace periods. The interest rate is determined annually, and reflects the cost of funds raised by the IDB on the world capital markets plus a small spread—typically 0.5%, but lower in 1985—to cover other costs. In 1985, the US dollar interest rate was 9½%. Loans made in local currency bear a much lower interest rate (4% in 1985). Loans also carry commitment and supervision and inspection fees. The terms and conditions of loans from capital resources are broadly equivalent to those set by the World Bank. Loans from the FSO have longer amortisation periods, ranging from twenty to forty years, with grace periods of five to ten years; they bear interest rates of between 1% and 4%, depending on the project and the level of development of the borrowing country. Loans made by the IDB are generally guaranteed by the government or an appropriate national institution of the borrowing country.

Sectoral and country distributions of lending

Provisional figures indicate that the IDB authorised loans of $3.1 billion in 1985, bringing the total of loans authorised since its inception to over $30 billion. In 1984 alone—the last year for which complete data are available—the IDB approved seventy-five loans totalling $3.6 billion; actual disbursements of previously authorised loans amounted to $2.4 billion, or $1.8 billion net of repayments. In fact, in terms of net disbursements, the IDB lent about as much to Latin America and the Caribbean in 1984 as did the World Bank.

The IDB's record as a catalyst for the mobilisation of external and domestic investment resources is good: it has participated in over 1,500 development projects with a total investment of over $100 billion. The IDB was the first international institution to venture into the financing of rural development projects on a large scale. Initially, the IDB's loans were concentrated on agrarian reform, land settlement, the provision of potable water supplies and rural roads. In the late 1960s and the mid-1970s, these efforts were expanded to include support for the productive efforts of small-scale farmers, through irrigation, farm credit and marketing programmes. Since then, the emphasis of the IDB's lending programmes has been on the provision of social services and the development of energy and, to a lesser extent, tourism sectors. The sectoral distribution of IDB loans at the end of 1984 is shown in Table B.

Table B
Sectoral distribution of loans approved

$ millions; *percentages in italics*

	1984		1961–84	
Productive sectors				
Agriculture and fisheries	865	*24.3*	6,319	*22.8*
Industry and mining	695	*19.5*	4,333	*15.6*
Tourism	37	*1.0*	296	*1.1*
Physical infrastructure				
Energy	899	*25.2*	7,380	*26.6*
Transportation and communications	362	*10.1*	3,511	*12.6*
Social infrastructure				
Environmental and public health	265	*7.4*	2,472	*8.9*
Education, science and technology	25	*0.7*	1,288	*4.6*
Urban development	297	*8.3*	1,086	*3.9*
Other				
Export financing	66	*1.9*	583	*2.1*
Preinvestment	24	*0.7*	335	*1.2*
Other	32	*0.9*	169	*0.6*
Total	**3,567**	*100.0*	**27,772**	*100.0*

Generally, the countries with the biggest economies have received, in absolute terms, the largest amounts of IDB loans (Table C). The main exception is Venezuela, which did not borrow from the IDB during the 1970s. However, relative to the size of their populations, the eighteen borrowers that are either regarded as less developed or considered to have limited markets—Bahamas, Barbados, Bolivia, Costa Rica, the Dominican Republic, Ecuador, El Salvador, Guatemala, Guyana, Haiti, Honduras, Jamaica, Nicaragua, Panama, Paraguay, Suriname, Trinidad and Tobago and Uruguay—have greater access to IDB finance than the largest regional economies. Thus, although the eighteen countries account for only 15% of Latin America's population, they have received 30% of total IDB loans and 50% of total FSO loans. This emphasis was amplified in the Sixth General Increase of Resources when it was agreed that, in the 1983-86 period, foreign exchange held in the FSO would be lent only to the ten least developed countries and that a limit ('cap') would be placed on the amount of capital loans made to the four biggest economies—Argentina, Brazil, Mexico and Venezuela.

Table C
Cumulative loan approvals by the IDB in 1961–84: country analysis

$ millions; *figures for disbursements in italics*

Country	Total		Detail by source of funds		
			Capital	FSO	Other funds
Argentina	3,502	*1,703*	2,467	538	48
Bahamas	5	*5*	3	—	2
Barbados	102	*60*	53	37	12
Bolivia	989	*508*	306	641	42
Brazil	4,731	*3,150*	3,481	1,110	140
Chile	1,798	*1,045*	1,552	203	43
Colombia	2,501	*1,290*	1,792	646	64
Costa Rica	764	*428*	338	361	65
Dominican Republic	955	*459*	306	582	67
Ecuador	1,426	*625*	671	663	91
El Salvador	707	*521*	232	374	101
Guatemala	798	*499*	250	487	61
Guyana	158	*94*	53	99	6
Haiti	224	*158*	—	214	10
Honduras	698	*512*	163	471	64
Jamaica	409	*228*	202	156	52
Mexico	3,213	*2,399*	2,625	553	35
Nicaragua	459	*375*	86	318	56
Panama	620	*479*	311	271	39
Paraguay	541	*302*	140	390	11
Peru	1,606	*959*	1,002	464	140
Trinidad and Tobago	19	*19*	—	19	—
Uruguay	510	*210*	380	96	35
Venezuela	774	*296*	600	101	73
Regional loans	771	*471*	499	191	21
Total	**27,772**	***16,794***	**17,512**	**8,984**	**1,277**

The lending programme since the emergence of international debt problems in 1982

Although the sectoral distribution of lending in the period covered by the Sixth General Increase of Resources has not changed radically from the pattern established in earlier years, there have been several developments that have represented major departures from previous practice. Some of these predate the entering into effect of the Sixth General Increase—13 December 1983—and some of them have occurred since then. However, the common theme is that they are all responses, either direct or indirect, to the advent of the international debt problem.

The first development was the creation of the Special Operating Programme (SOP) in April 1983. The goal of the SOP was to lend effective and timely support to countries readjusting their economies in the wake of the debt crisis: in particular, to enable completion of high-priority IDB projects where the recipient country is facing difficulties in executing the project because of prevailing economic conditions (eg shortage of external or domestic finance to supplement IDB funds). The measures comprising the SOP—sometimes called 'flexibilisation' measures, and analogous to those incorporated at the time in the World Bank's Special Action Programme—included accelerating the flow of disbursements to projects, providing extra financing, redefining project goals, and financing cost overruns. The SOP has been extended into 1986.

In December 1983, and as part of the agreement for the Sixth General Increase of Resources, a new Intermediate Financing Facility was set up. Funded from the FSO's general reserve, the facility is used to defray up to 5% per annum of interest charges on loans from the IDB's capital to the eighteen less developed and limited-market countries.

Finally, in May 1984, the Industrial Recovery Programme (IRP)—which was originally set up in 1982 to finance imported inputs to exporting industries in the eighteen less developed and limited-market countries—was extended to all borrowing member countries. Its rules were amended and it was envisaged that up to 15% of lending from capital would be allocated to the IRP. Amortisation periods were lengthened and the priority accorded to export industries facing foreign exchange constraints in the original policy was qualified. Loans under the IRP have been likened to World Bank structural adjustment loans (SALs) in that neither are specifically related to 'projects'. However, IRP loans differ significantly from SALs in that they are disbursed in one payment and the emphasis is on infusing foreign exchange rather than on eliciting wider policy changes in the borrowing country.

The Inter-American Investment Corporation

In November 1984, representatives of the majority of IDB member countries completed negotiations on an agreement establishing the Inter-American Investment Corporation (IIC), a new IDB affiliate. Member countries have until the end of June 1986 to sign the agreement. The purpose of the IIC is analogous to that of the International Finance Corporation, a member of the World Bank group: to encourage the establishment, expansion and modernisation of private enterprises, particularly small and medium-size concerns. It will do this in the main by making direct investments in those enterprises and encouraging other potential investors to do so. It will also strive to strengthen domestic capital and other financial markets. If successful, the IIC will be instrumental in helping to reduce, albeit in a small way, the dependence of Latin America on non-equity external finance. The IIC will have an initial paid-in capital of $200 million, although the charter provides for the issue in future of callable capital. The capital shares of the IIC will be divided as follows: regional borrowing countries, 55%; United States, 25½%; other countries, 19½%. So far a number of countries outside Latin America, including Canada and the United Kingdom, have decided not to subscribe to the IIC at this stage, although they may take the opportunity to do so in the future.

Technical co-operation functions of the IDB

The IDB contributes to the economic development of Latin America in ways other than by lending. It provides technical co-operation for the preparation, financing and implementation of development plans and projects, and for strengthening economic institutions. This role is established under Article VI of the Articles of Agreement. By the end of 1984, the IDB had approved a total of $1.1 billion for technical co-operation, of which $0.5 billion was on a grant or contingent recovery basis, and $0.6 billion on a reimbursable basis.

Lending and economic reform: the future role of the IDB

In October 1985, US Treasury Secretary James Baker made a number of proposals designed to allow more scope for Latin American (and other developing) countries to 'grow out' of their problems in a non-inflationary way. Under Secretary Baker's proposals, although the IMF would continue to play a central role in helping countries to adjust their balance of payments, the extra emphasis on non-inflationary growth would require a greater role by the World Bank and the IDB in the provision of finance for soundly-based programmes of economic reform. To this end, it is proposed that the World Bank and the IDB should increase disbursed lending by 50% in the next three years over previously programmed levels and that the IDB should channel a proportion of its funds into structural adjustment and policy-based lending. In other words, the IDB would emulate and, indeed, co-operate with the World Bank in making a significant proportion of its loan disbursements conditional on policy reforms and institutional changes. Although the IDB is already involved in non-project lending, the emphasis to date has been more on increasing the flows to Latin American and Caribbean countries to give short-term support for balance of payments purposes. It is possible then that, in the future, there will be more emphasis on linking loans to the sort of economic conditions that would help make borrowing countries' balance of payments sustainable in the medium term. These issues are currently being discussed in the context of the negotiations on the Seventh General Increase of Resources, which will cover the three-year period commencing 1987.