SUMMARY PRESENTATION

by

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INTRODUCTION

It is a great pleasure to find myself this morning among this distinguished group of government officials, bankers, pension fund managers and insurance representatives. As you know, in all countries, all these personalities mentioned play an import role in helping to achieve the economic objectives of their clients and the societies where they operate. The Bank in its Treasury side has much in common with that experience. The World Bank is a bank in the sense that it intermediates the flow of funds; that is, the Bank borrows funds from the private capital markets and lends them to developing countries through the operations of its projects and loan officers. About 70% of every loan that is committed and disbursed to developing countries will be funded through borrowings.

As a bank, therefore, the Bank manages its financial affairs in a prudent fashion in order to assure itself support in the private markets on which it depends. The Bank is managed, in part, to meet the requirements of the most conservative savers in the financial markets. On the other hand, the World Bank is an international public institution. Its shareholders are the governments of the world and the Bank must manage its affairs in accord with their guidance and in an objective and professional way that will permit governments to discuss and agree on policies for running an institution in

which they all share responsibility. Finally, the Bank has a third constituency -- the less developed countries which are both shareholders and its borrowers. The Bank's purpose, as I am sure you know, is to promote economic development in the less developed countries and everything it does -- in the private sector and in terms of its recommendations to its shareholders -- is framed with the view towards providing the funds required by the less developed countries at the lowest possible cost on an ongoing basis in order to help them meet their goals of economic development, and thereby support growth in the world economy.

BALANCE SHEET

What I would like to do at this time is spend a few moments to review with you the balance sheet of the World Bank as a means of explaining how the Bank conducts business on its financial side. What I hope to convey to you is not only the large size and conservative structure of the World Bank but also a sense of how the Bank is managed in ways that achieve a balance between the interests of the three constituencies I mentioned -- the private marketplace on whom the Bank depends for funds, its shareholder governments on whom it depends for its continued support, and the less developed countries for whom, after all, it exists to underpin their economic growth.

The Bank has a straightforward balance sheet which I would like to review with you. The figures I use are as of December 31, 1985. Basically, there are only a few major items on each side of the balance sheet adding up

to $82.6 billion. For purposes of this presentation, it is convenient to focus only on the most important assets and liabilities, and to net out the minor items. When this simplification is made, then the total balance sheet is $72.9 billion 1/. On the asset side, the Bank has mainly cash and loans, and on the liability side, its borrowings, capital and reserves and accumulated net income. I think in each of these areas, you will find the Bank is unique in its approach to financial management. Let me say at the outset that the Bank's balance sheet is different from any private institution whose paper you may hold. It is an exceedingly conservatively leveraged financial institution.

(A) ASSETS

On the asset side, on December 31, 1985, the cash liquid assets of the Bank stood at $19.9 billion. The Bank has a policy of maintaining this extraordinary high level of liquidity in order to assure flexibility in borrowing decisions. This liquidity was equivalent to 32% of all outstanding Bank debt and was equal to 90% of the debt issued by the Bank to private investors, maturing within 5 years.

1. Liquidity

Under its current policy the Bank aims at keeping its cash and liquid investments in the range of 40-45% of its projected net cash requirements for the next 3 years. Presently, liquidity is almost 6 times short-term debt and represents over 45% of the Bank's next 3 years of net disbursements. The Bank holds this liquidity for one reason — flexibility. The Bank wants to be able to borrow when and where it thinks it's wise.

And it wants to have the cash on hand to stay out of markets when the costs are too high or when markets are unstable. It is built up when markets are stable and open and held until needed on disbursements.

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Summary Balance Sheet

December 31, 1985
(Dollar amounts in billions)

Liquidity	19.9	Outstanding debt	61.3
Loans Disbursed	51.9		
Other assets net of other liabilities	1.1	Capital & reserves & accumulated net income	11.6
	72.9		72.9

That liquidity, which stands at almost $20 billion as compared to about $1.3 billion 13 years ago, was deliberately built up by what one might call "excess" borrowing. It was built up so that the Bank would have the flexibility to decide when it borrows, where it borrows and how much it borrows. The Bank does not want to be in the position of having to borrow when it would prefer to wait 6 months. The liquidity policy serves that function. Thus the Bank systematically has increased its liquidity position by borrowing substantially in excess of its current requirements at times when funds were obtainable at what it considered reasonable costs and terms of maturity. The Bank does not wait until it needs resources to meet its requirements. Rather, it anticipates those requirements and holds liquidity.

Let me take the opportunity to talk for a few moments about that $20 billion in liquidity; for indeed, the Bank is not only a large borrower in the market, it is a rather significant investor in tdhe

marketplace. Since it does not take a currency risk when it borrows dollars, Deutsche Mark, Swiss Francs or Yen, or any other currency, the Bank invests them in a wide variety of instruments -- ranging from 1-day money to 5-year bonds pending disbursement on loans. The portfolio of the Bank's liquid resources is actively managed. The liquidity is in 30 currencies or currency units, though about 75% is in dollars. All of it could be converted to cash to meet the Bank's commitments in about 48 hours.

The Bank's goal is rather simple. Since it has the liquidity which is designed to give it flexibility as to when to borrow, the Bank wants to manage that liquidity (even when there is a positive yield curve) so that the short-term investments will produce a rate of return that offsets the cost of borrowing long-term funds. That means the funds must be managed. In short, the Bank does not want the holding of its liquidity to be costly. That involves some management procedures, techniques, policies and philosophy which I would like to share with you. You may find it relevant to your own operations.

The rules of the game should be straightforward.

1) A security, once purchased, is always available for sale;
2) The portfolio is managed with a view toward obtaining the highest potential future financial rate of return;
3) The staff is to pay no attention to the book cost of a security after it is purchased in determining whether or not to sell it. Book cost is a past event; it tells us nothing about whether we should hold a security or sell it;

The Bank has open lines to about 20 firms throughout the United States. It has daily telephone communications with the largest banks and dealers active in each European market. It develops in-house forecasting models using financial variables such as money supply, Federal funds, foreign exchange, and "real economy" variables (e.g., business loans, housing starts, retail sales, CPI, etc.). In short, the Bank tries to bracket interest rates, and does so for a variety of maturities and instruments and varying probabilities. Then the Bank makes investment decisions with respect to how it wants its liquidity invested.

Let me underline one fact. The liquidity is profitable, but even if it were not, the Bank would hold it because it is a basic premise of its financial policies to be prudent -- which means to maintain flexibility -- that is, to draw it down and build it up -- opportunistically. The rate of return for the first half of FY86 is 11.23%. The Bank's liquidity consistently produces returns higher than its cost of debt.

2. Loans

The Bank's other asset is its portfolio of outstanding loans which are made to support economic development in member countries of the Bank. All loans by the World Bank are sovereign credits. All are guaranteed by the government where the funds are lent. Loans made by the World Bank since 1946 to December 31, 1985, totalled $117.6 billion of which $27.4 billion has already been repaid. On December 31, 1985 loans held by the Bank totaled $90.2 billion, 58 percent of which

(about $52 billion) was disbursed and outstanding to be drawn down by borrowers over the next six or seven years; the remainder (about $38 billion) was committed but undisbursed awaiting project progress. This makes the major difference between the World Bank and a commercial bank. This great lag between commitments and disbursements is one thing that distinguishes the Bank from banks and other private lenders. The Bank does not simply transfer funds. It makes payments over a long time to assure orderly completion of projects. It also has a large staff to audit the business relating to a project before it makes disbursements under its loans.

The Bank's loan portfolio is diversified by country and project sector. No loans are made in countries not deemed creditworthy and country creditworthiness of all borrowing members is kept under continuous review. The overwhelming proportion of Bank loans is in support of individual projects to promote the economic development of member countries. These projects must produce acceptable rates of return to the borrower; they must be of high priority in the country's development program/strategy. Loans, as I mentioned earlier, are typically disbursed over a period of 5 to 7 years against documented expenditures reviewed by the Bank. Bank loans are used primarily to finance goods and services procured under international competitive bidding, and most payments are made directly to outside suppliers of goods and services. Typically, a Bank loan covers less than half of the overall costs with the balance coming from borrowers' resources and external loans. During the past calendar year, the Bank committed about $11 billion in development loans, and expects to commit about $12 billion in FY86.

In addition, the Bank engages in policy-based lending in the form of structural adjustment and sectoral adjustment loans. These programs account for 10-15% of present and projected commitments.

The Bank has never suffered a loss on a loan or any write-offs. While it has experienced some delays in repayment of principal and in payment of loan service charges, it has never had a default. It has a firm policy of not participating in rescheduling. It does not change the terms of its loans and it does not refinance them.

The return on average loans outstanding for the six months ended December 31, 1985, averaged about 9.14%, which included a commitment fee, and an interest rate which is based on the cost of the Bank's debt. Loan charges currently include 1/2% spread over the cost of borrowing, an interest rate of 8.50% and a commitment fee of 3/4% on undisbursed loan balances ($38.3 billion). The Bank's income is exempt from taxation.

The reasons for this <u>impeccable</u> record are many. You may ask: Why have borrowers maintained such excellent financial relations with the Bank?

1. The Bank pays great attention to the rate of return and viability of the project. Borrowers realize that and want to maintain the flow of technical expertise.
2. On the Bank side, as I have said, there is an enormous expenditure of time, effort and money on evaluating a country's creditworthiness. We simply do not lend to countries if our economists believe a country is not creditworthy.

3. The bulk of the Bank's administrative budget goes to determine whether a project makes sense, whether a country is creditworthy and to perform the economic and sectoral analyses necessary to provide the underpinning for our loans, and to supervise those loans during the 6 or 7 years disbursement periods. We are now supervising over 3,000 loans. Borrowers do not want to lose that tremendous resource.

4. If a country is 30 days late on an interest or principal payment, for any reason, all member countries are notified of that fact in writing through the Bank's Executive Directors. Borrowers do not welcome that kind of publicity.

5. As I have said, the Bank is a long-term lender -- we will simply stop disbursing on all undisbursed loans if a country is 75 days late on any of its obligations.

6. No new loans or appraisals of possible future loans will be made until the deficiency is corrected.

7. If the amount is material, we will advise the world by putting it in our prospectus.

8. The borrowing country also sees something for its indebtedness -- a project on site -- a valuable asset.

9. Most important, however, LDCs trust the Bank's objectivity, its technical expertise and the non-political nature of its lending. They do not wish to jeopardize either the flow of advice or resources from a dedicated staff committed to the country's economic development.

In sum, the Bank is trusted and has developed long standing relationships. On the other hand, if there were a significant break in repayments, the Bank stops all disbursements on all the respective projects -- and, as I have noted earlier the Bank has almost as much in undisbursed funds as in those outstanding. Finally, the Bank is an instrumentality of its member governments. A rupture with the World Bank would be a break with the world's financial system. And no country wishes to risk that.

At this point, before talking about the liabilities of the Bank, I would like to say a few words about the Baker Plan. We believe it is essential to provide additional external capital to foster growth in heavily indebted countries. If reform programs are to be workable and structural adjustments are to take place, a particular country needs to sustain a certain growth path and the implementation thereof must take place in cooperation with commercial banks and the International Monetary Fund.

B. LIABILITIES

Now let me turn to the liability side of the Bank's balance sheet.

1. Borrowings

The Bank's borrowings at December 31, 1985, were $61.5 billion. These borrowings were denominated in 20 currencies or currency units and carried an average cost for the six months ended December 31, 1985 of 8.37%. Indeed, the cost of total borrowings and other funds available during the first half of FY86 was only 7.22% after swaps. Most of the borrowings were originally contracted as medium- or long-term fixed rate

obligations. The Bank enjoys access to capital markets worldwide on the basis of its reputation as a premier credit. The Bank's Discount notes are traded along with the securities of US government agencies in the sector of the market known as the "agency market", where credits are so fine that the paper is not even rated. The Bank's medium and long-term US publicly issued notes and bonds have been rated AAA/Aaa by Standard & Poor's and Moody's -- the rating agencies. Securities issued outside the United States without ratings have been at yields comparable to government or government guaranteed debt, whenever there is no distinction between domestic and foreign markets.

The Bank is a major borrower in world-wide capital markets. It is the largest non-resident borrower in highly conservative markets such as Switzerland, Germany, Japan, and the Netherlands. The Swiss capital market in particular, is very important to the Bank. In CY 1984 the World Bank borrowing share was 13.5% of the total SwF 40.6 billion foreign capital market. To date, the Bank has borrowed in the Swiss franc as a currency SwF 30.1 billion in private placements, syndicated loans, direct loans and public issues, of which about SwF 20.4 remains outstanding.

Considering that the World Bank first entered the Swiss capital market in 1951 with a bond issue of SwF 50 million, this growth represents a considerable achievement which reflects on the support it enjoys with underwriters, the banking community as a whole, its institutional investors and private investors in this country. I should also stress that the Bank would never have been able to attain this level of borrowings without the full support of the Swiss financial authorities and particularly the Swiss National Bank and the Swiss Government.

The Bank follows a policy of diversifying its borrowings by currency, country, source and maturity to provide maximum flexibility in funding. Indeed, of the Bank's outstanding debt - medium, long-term and short-term of $61.5 billion, there is $20.2 billion in US dollars, $13.1 billion equivalent in Yen, and $10.2 billion in DM and $9.8 billion equivalent in Swiss Francs. Other currencies amount to $8.2 billion. The Bank does about 150 separate borrowings a year. The Bank's liabilities in each currency are matched by assets in the same currency. Finally, on December 31, 1985, $8.3 billion, or about 14% of the Bank's medium- and long-term debt was held by central banks or other government authorities.

The Bank is no less a development agency because its liability management is similar to the private sector. It is the asset side which makes it a development agency.

Today, the Bank is in a very strong position, not only because of its profits but because it has been able to fund its expanding needs from the capital markets.

The success of that process is seen in the borrowing and investment programs' contribution to the Bank's mid-FY86 financial results. The Bank has borrowed the equivalent of $6.8 billion -- a record amount.

Borrowing costs were lower than for the same period last year. Currency swaps have helped bring down these costs, and so has the timing of issues, choice of currencies and some new techniques or financial engineering.

First Half FY86 (July 1 - December 31, 1986)
(US$ equivalent, millions)

	Amount	Average Cost (%)
Medium- and Long-Term		
Fixed Rate		
Before swaps	6,537	7.94
After swaps		7.22
Floating Rate	-	
Additional Short-Term		
Central Bank Facility	250	8.10
Total	6,787	7.25

Borrowings By Currency*	Before Swaps Amounts	Before Swaps %	After Swaps Amounts	After Swaps %
U.S. dollars	1,596	24	1,026	15
U.S. dollars (increase in outstanding Central Bank short-term borrowings)	250	4	250	4
Deutsche mark	862	13	1,140	17
Swiss francs	1,267	19	1,910	28
Japanese yen	1,274	19	1,367	20
Dutch guilders	528	8	658	10
Austrian schilling	52	1	-	0
Belgian francs	114	2	9	-
Canadian dollars	147	2	60	1
ECU (European Currency Units)	342	5	178	3
Norwegian kroner	30	-	30	-
Pounds Sterling	131	2	131	2
French francs	107	2	6	-
Danish kroner	53	1	0	-
Luxembourg francs	6	-	6	-
Italian Lire	28	-	28	-
Total	6,787	100	6,787	100

* Medium- and Long-Term (MLT) Fixed-Rate borrowings, except where indicated.

The Bank's reputation in the capital markets is better than ever, and it has been able to borrow at the narrowest spreads ever achieved.

With respect to new techniques the World Bank achieved a SwF 600 million Zero coupon issue for 30 years, which was qualified by Agefi as the Swiss franc issue of the year. The availability of very long maturities in the Swiss capital market is certainly a very welcome development, with in particular our last 30 year straight conventional public issue - the longest maturity of its kind in this market.

As far as swaps are concerned we have implemented an insurance program for swaps to enable the Bank to broaden the range of elibigle counterparties. The Bank plans to start this program in the near future. Under this scheme, upon the default of a counterparty, which is unlikely because of our credit selection, and the resulting early termination of the swap, the insurance company would have to pay the Bank the net settlement amount as defined under the respective swap contract. This program essentially permits the Bank to negotiate swap terms directly with the ultimate counterparty.

2. Capital

The Bank has two kinds of capital pledged by member governments. On December 31, 1985, the paid-in capital of the Bank stood at $5.8 billion. In addition, the Bank has made a profit every year and its accumulated reserves are not distributed as dividends -- they are put back to work at

the Bank. As of December 31, 1985, the Bank had reserves equal to $5.86* billion. Therefore, the total of paid-in capital and reserves of $11.6 billion results in a debt/equity ratio of 5.3 to 1.

The average cost of total funds -- debt plus equity -- was 7.22%. I think you will agree that those are very conservative ratios, unknown to commercial banks or, for that matter, worldwide government agencies. And that may be compared to the return on the Bank's average earning assets -- its liquidity and loans -- which together return 9.79% or a spread of 2.57% over the cost of total funds.

The Bank is managed as a prudent and profit making institution, viable as far into the future as we can see. The Bank has earned profits every year since 1946. Net income for the fiscal year ending June 30, 1985 was $1.1 billion and so far for the first half of FY85 the Bank has earned more than half that amount -- exactly $695 million and the Bank is headed for another record year. In summary, the profitability of the Bank results from several factors. The overall cost of funds to the Bank is comparatively low, representing the blended cost of diversified borrowings; and substantial paid-in capital, reserves, and retained earnings. Substantial profitability is also derived from the return on actively managed liquid assets and the policy of pricing loans to cover borrowing costs, administrative expenses and to earn a reasonable return on equity.

*		
	General reserve	$4,769 million
	Special reserve	293
	Accummulated net income	695
		$5,757

Since very little of the Bank's lending is funded by member governments -- more than 90% of funds are internally generated and borrowed from the private sector and government sources at market-based rates -- profitability is very important. Profits demonstrate to the markets the Bank's financial strength, and because of this strength, the Bank can borrow and lend to developing countries at the lowest possible rates.

It is the Bank's financial strength that has allowed it to reduce charges to developing countries. Within this context, last year the Bank decided to reduce the front-end fee to zero, and on January 1, 1986, the lending rate was lowered from 8.82% to 8.50%. (Its an annual rate adjusted semi-annually).

There is one last piece in the uniquely conservative structure of the Bank. The paid-in capital is the tip of the iceberg. Member governments are obligated to provide more than 10 times their paid-in capital to the Bank on a contingency basis. It is called Callable Capital. On December 31, 1985 callable capital of member governments stood at $61 billion. Callable capital is solely for the protection of bondholders and can only be used for that purpose. The callable capital may not be used in Bank operations for disbursements and the Bank may only require a call on the callable capital if it is unable to meet its obligations on its bond or noteholders in full, out of its other assets. And that is not about to happen and never has. But more, the Bank is presently implementing a capital increase which, proforma, would raise our capital to about $86 billion.

And, as you know, under the Bank's original charter (the Articles of Agreement), the Bank is limited to a ratio of 1:1 of outstanding and disbursed loans ($51.9 billion) against the sum of paid-in and callable capital, reserves and retained earnings which now total $72.6 billion.

There is no parallel in the private marketplace. The Bank is under leveraged as a result of its institutional history. It cannot have loans outstanding greater than its capital and reserves i.e. 1:1 restriction. From the standpoint of the countries who need the Bank's support this is, no doubt, an undue constraint. But for the marketplace I hope you will agree that it makes the World Bank a credit second to none.