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Opening Address by the Chairman,
the Hon. **WOLFGANG RUTTENSTORFER**,
Governor of the Fund and the Bank for **AUSTRIA**,
at the Joint Annual Discussion

Opening Address by the Chairman of the Board of Governors

I am honored, on behalf of Austria, to chair these 1998 Annual Meetings of the World Bank Group and the International Monetary Fund. Before addressing the issues before us, it is a pleasure for me to extend a special welcome to the delegation of the Republic of Palau, attending these Annual Meetings in the capacity of member for the first time.

These meetings take place against the backdrop of the most serious crisis facing the international economic system in over a generation. While it started in one part of the world, through contagion it spread to others. This turmoil compels us to redouble our efforts in overcoming the crisis through strengthened international cooperation. The attention of the world is focused on our deliberations, so let us move forward to take up these challenges and fulfill our international obligations.

My fellow Governors,

As we stand here in the twilight of the millennium and in the midst of these uncertain times, we might well ask ourselves where we—the international community and the membership of the Bank and the Fund that comprises it—are headed.

Does the past provide a useful guide for the future? The post-war period has been a remarkable and unique period in human history. For the first time, we have, in the shape of the U.N., the Bretton Woods institutions, and recently the WTO, organized fora for international cooperation on a global scale. This has included a gradual opening to new members and in particular the transition economies into the Bretton Woods Institutions, to make them truly universal.

These fora have helped to institutionalize cooperation—a powerful instrument for promoting global prosperity—well before the term

"globalization" entered our lexicon. They have allowed us to deal with and adapt ourselves to the challenges of international developments that threatened the well-being of a significant portion of our membership. To mention only a few: the end of the par value system, the oil shocks of the 1970s, the debt crisis of the 1980s, the transition from centrally planned economies to market economies, and, more recently, the Asian crisis.

The architects of the post-war international financial system provided us with a house with solid foundations, strong walls, and a stable roof.

We are today being asked the question: Is yesterday's architecture adequate for tomorrow's challenges? Having my office in a building in Vienna that dates back to the beginning of the 18th century, I would tend to be architecturally cautious—evolutionary rather than revolutionary.

What is even more important than the architecture of a house is how the people inside behave towards each other and how they resolve conflicts. Here, we have good principles that have served us well over the past decades: Cooperation, democratic principles, predictability and accountability

towards each other. We, therefore, need to build on this foundation to strengthen the architecture of the international financial system, adapting it to new challenges.

European Economic Monetary Union

The international economic and financial system is evolving rapidly. One major quantum change in international monetary relations is less than three months ahead of us. The launch of European Economic and Monetary Union this coming January 1999 will constitute one of the most significant changes in the international monetary system during this century. Underpinned by strong fundamentals and sound economic policies, the euro has the potential to become a major vehicle currency in international trade and a major official reserve currency, as well as enjoying a strong role in private sector portfolios.

Prospective euro-area members have worked hard to ensure that the single currency will strengthen the European economy, as well as the world economy. Euro-area members have agreed to adhere to a stability-oriented policy framework, including a commitment to price stability and prudent fiscal

policies, as well as concerted structural reform efforts, especially in the areas of labor and product markets. We are convinced that by complementing the single market, the Monetary Union will improve growth and employment prospects in Europe, and will have positive spillover effects for the world economy. Also, by developing deep and highly liquid integrated financial markets, all investors will benefit from more opportunities and greater efficiency. Thus, the euro can be a stabilizing factor for the global financial system as a whole.

In this context, a solid relationship between the euro area and the Fund, between a region of stability and the world economy, combining regional cooperation and a global perspective, is crucial. We welcome the ongoing efforts to establish the appropriate institutional arrangements between the Fund and euro area.

In keeping with the need to foster cooperation, both regionally and globally, the European Union is also reaching out towards the transition economies of Central and Eastern Europe. The process towards EU enlargement marks a new quality of European integration and provides a framework for the further

transition of these countries towards strong and stable market-based economies.

The Fund and the Bank have supported the bold reform efforts of the transition economies, and they will continue to play a vital role in assisting their further integration into the world economy.

Benefits and Risks of Globalization—Recent Crises

Integration into the world economy such as the transition economies have been experiencing, nowadays called globalization, can provide enormous potential for growth and prosperity. The Austrian experience is a case in point, highlighting in particular the importance of international integration for small economies. For the past decades, Austria has successfully pursued a strategy of international openness, culminating in the accession to the European Union nearly four years ago.

The adoption of an outward-oriented approach, underpinned by an exchange rate policy geared at maintaining stability vis-à-vis our biggest trading

partner, has contributed to modernizing our industries, maintaining low rates of inflation, and achieving a steady medium-term growth path. In the last years, globalization requirements, but also the preparation for the Monetary Union have resulted in policies which have led to unprecedented price stability, a move towards a balanced budget and strengthened growth performance. Within the euro area—that is within a strong economic and trading area—small countries like Austria will more easily meet the challenges of increased competition stemming from further globalization.

While the potential benefits from globalization are widely accepted, we see the potential for destabilizing risks in those countries unable to withstand the stress of the dynamic forces of globalization.

Since we met last year in Hong Kong, developments in some parts of the world economy have taken a turn for the worse. Recessions in several Asian economies have deepened. The recent crisis brought to the forefront deep-seated problems in many countries, particularly weaknesses in the banking and financial sectors, weak supervisory and regulatory systems, and lack of good corporate governance. Recent developments in Russia have been

worrying. Contagion effects have been compounded by homemade problems, such as poor fiscal policy performance and the failure to address structural weaknesses in the financial sector, but also in the real economy.

We must realize on the other hand that also countries with essentially sound policies have been affected by the crisis, as markets do not always seem to be sufficiently aware of country-specific circumstances. In finding ways to prevent and resolve such crises, an essential condition is to rectify weaknesses in the countries themselves and the pursuit of sound domestic policies to make them resilient to external shocks.

However, we need to go beyond that. Global problems need global answers. We need to see what we—the international community—but also, importantly, the private sector, can do. Therefore, a major challenge before us is to adapt the international financial system to better respond to the realities of today and the challenges of globalization in future years.

Although much more needs to be done, work has already progressed in a number of areas toward reinforcing the international monetary and financial system.

First, information and transparency are central. In order to improve the functioning of financial markets and the conduct of Fund surveillance over members' policies, the availability and transparency of information must be enhanced. Timely disclosure of economic data and policies is important for lessening the likelihood of crises and reducing their severity when they occur. International capital markets, in order to function effectively, also need comprehensive and timely information. To that end, we look forward to further initiatives at increasing transparency, while paying due respect to the role of the Fund and the Bank as trusted advisors to members.

Second, while more transparency and information are necessary, they are not sufficient. Globalization has increased the vulnerability of domestic and international financial systems to potential shocks. A clear lesson from the recent crisis is that we must strengthen the supervision of financial systems. In this regard, standards in banking supervision, data dissemination, fiscal

transparency, monetary and financial policies, bankruptcy, corporate governance, and accounting have an important role to play in strengthening national and international financial systems. This would allow market participants to compare information about a particular country's practices. We welcome the ongoing work in the Fund and the Bank and in other organizations and fora on this important matter.

Third, work has also moved forward in considering ways to more fully involve the whole international community, including the private sector, in preventing and resolving financial crises. We need to think creatively about ways to respond to acute short term liquidity crises, particularly those generated by a generalized loss of market confidence rather than by economic policy failures in the countries concerned.

One aspect of this, as I mentioned above, is involving private creditors at an early stage. This could help to achieve an equitable burden sharing vis-à-vis the official sector, and to limit moral hazard. Private sector creditors must recognize their responsibility to remain engaged in a country's economy during times of crisis. Another aspect is a good look at ways the international

community as such can respond better to the challenges it faces, and at the financial institutions that deal with those challenges. Greater openness and accountability of countries also necessitates a corresponding effort by international financial institutions.

Many efforts in that direction have already been made, but we must do our best to improve the cooperation between international financial institutions, to improve the public perception of their activities and to take fully into account the impact on the poorest sections of society.

Fourth, the trend toward greater mobility of capital across borders is here to stay. The transfer of capital on a long-term basis also brings with it other benefits in terms of access to technology and skills. At the same time, we would all agree that we need to work to make countries more resilient to possible shocks arising from volatile capital movements. To that end, liberalization of capital flows must proceed in a prudent and properly sequenced manner in order to maximize the benefits and minimize the risks. The pre-conditions for liberalization, especially a sound financial system, must be well in place first.

Efforts at Assisting the Neediest Members

Whilst reflecting on the architecture of the international monetary system is important, let us not forget that, in the midst of and due to this financial crisis, there is an ongoing human crisis as well. Millions of lives have been affected.

The impact has been felt most severely by the most vulnerable in the countries involved—the poor, and in particular, the women and children. Because unemployment is on the rise and incomes have fallen, poverty is increasing at an alarming rate. The poor will suffer from the irreversible losses in potential education and health that will impede their participation in future recovery. An increase in social unrest, crime and violence has also resulted from this crisis.

In the short term, the poor must be protected against drastic declines in consumption. Measures should aim at ensuring food security and preserving the purchasing power of vulnerable households. In the long term, appropriate social safety nets will need to be created.

The Bretton Woods Institutions are increasingly mindful of the social aspects of crises. In particular, the Bank is assisting governments to manage the social consequences of the crisis by protecting and improving the quality of social services and public expenditures targeted to help the poor. This includes improving the design and financing of social funds; strengthening social security systems for the unemployed and the elderly, supporting labor-intensive projects; and addressing key institutional issues.

We must also ensure that the trend toward globalization does not impede the development of the neediest countries. In the spirit of solidarity and cooperation, we must support the bold adjustment efforts that these members undertake. In this context, the World Bank must continue to respond to the needs of its borrowing countries. The actual challenge is not only to protect the poor, but more than ever to support structural reforms and improvements in public and private sector governance to make countries more resistant to economic shocks. We also encourage the IMF and the Bank to continue their fight against corruption.

We welcome the progress achieved in implementing the HIPC Initiative. Only two years after this challenging and pioneering effort of the international community was initiated, seven countries have been included in this initiative, of which two have reached the completion point. We need to continue our cooperation and also to make progress in complementary assistance for countries emerging from conflict.

We must also pledge to ensure that a sufficient level of resources are made available for the proper functioning of the ESAF, and we should redouble our efforts to secure the necessary financing. We welcome efforts to strengthen the ESAF following the recent evaluations. We must ensure that countries adopting courageous policy reform programs aimed at sustainably reducing poverty receive strong donor support. IDA is a key instrument in support of the poorest countries. Reaching an agreement in the coming weeks on an IDA-12 replenishment is critical to demonstrate to the poorest countries—particularly those with sound social and economic policies—that their plight is not forgotten and their efforts will be supported, even as the world community responds to crises elsewhere.

Resources

The international community has assigned a central role to the Fund and the Bank in the international financial system and in fostering sustainable development. Against the background of present challenges their effectiveness needs to be enhanced. Essential to this goal is ensuring that they have sufficient resources to do their jobs.

The Fund's financial resources are at a precariously low level, limiting its ability to support members' adjustment efforts. Therefore, it is essential that the quota increase become effective as soon as possible. To strengthen confidence in the institutions' ability to respond to the crisis, the international community must live up to its obligations.

The Bank has recently taken actions to maintain its financial integrity. Its contributions to support recovery in East Asia and elsewhere and to provide necessary protection to the poor will be needed also in the future. To maximize efficiency and coherence, we need to make sure that our

institutions take account of their comparative advantages and respective mandates.

In addition to strengthening the Fund and the Bank with adequate financial resources, we must do more to support and advocate their work in our respective nations and ensure that they remain the central institutions for international economic cooperation. We must do more to explain carefully their vital work, in order to cultivate a broader and deeper understanding among our citizens. So many different fora are increasing their efforts to contribute to strengthening the international monetary system that it is difficult to keep track of their work. Let us not forget: we are here as the G-182, the centerpiece of international cooperation! This cooperation effort is crucial and the time has come to distill the lessons from these deliberations and to integrate the different building blocks into the central work of a new architecture.

Conclusion

My fellow Governors,

As you know, I come from Austria, a mountainous country, where we had to learn long ago how to deal with the perils and uncertainty of uncharted, terrain mountain territories. In such a situation, markers along the way are important in helping to orient ourselves. Much like in the deep snows of the winters in Austrian mountains, these markers may be hidden to us, but it is our duty to work to reveal them to the international community. We are all in that challenging situation now. We have a difficult time ahead of us, but I am certain that our common effort will lead us to resolve our problems in an equitable manner. Let us now, together in this Meeting, set those markers that will carry us through the difficult time ahead.