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Statement by the Hon. **VICTOR JOY WAY**,
Governor of the Bank for **PERU**,
at the Joint Annual Discussion

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Washington, D.C., September 29, 1999

1. Mr. Chairman, Governors, ladies and gentlemen: It is a great honor and privilege for me to address this assembly as the representative of Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, Dominican Republic, Ecuador, El Salvador, Guatemala, Guyana, Haiti, Honduras, Mexico, Nicaragua, Panama, Paraguay, Spain, Suriname, Trinidad and Tobago, Uruguay, Venezuela and my own country, Peru, on the occasion of the 54th Annual Meetings of the Governors of the World Bank and the International Monetary Fund.

Global and Latin American Economic Development

2. The countries of the region regard the slow but steady recovery of the global economy with hope and a certain measure of optimism. On the one hand, the United States continues to lead the world leader in economic growth, at the same time maintaining low inflation and a high level of employment. The European countries are showing signs of increased economic activity, Japan is emerging from recession, and the other Asian countries have succeeded in stabilizing their economies and resuming growth. The resurgence of these economies will contribute to renewed demand for our region's major exports and normalization of their international market prices.

3. Throughout 1999, the Latin American economies continued to be affected by deteriorating terms of trade and the reduction in capital flows that had begun in 1998. However, thanks to their sustained prudent policies and greater dynamism in the global economy, conditions have been created that can be expected to result in 3.9 percent GDP growth in the region in the year 2000. This achievement goes hand in hand with a continuing decline in the inflation rate. There can be no doubt that these improved prospects are ascribable to some extent to the positive developments in the economy of Brazil, which has managed, after a major effort, to reverse the conditions of uncertainty that prevailed a year ago and achieve a higher level of economic growth than initially projected.

4. On the other hand, elections are to be held in several countries in the region in 1999 and 2000. However, given the consolidation of our democratic systems and the fact that a consensus has emerged in favor of economic stability, we do not expect this heavy electoral calendar to be a cause of economic disruption. At the same time, we are aware that we are still at risk should there be adverse developments in the global economy —

such as an economic slowdown in the United States. On this score, we take a positive view of US preventive monetary policy measures, which will contribute to the stability of international financial markets.

5. The unforeseen, major shocks that many of our economies have had to contend with since mid 1997, not to mention the rapidity and extent of their contagion, have proved a sharp reminder that the individual countries, as well as the international financial system as a whole, need to strengthen existing preventive mechanisms. The Contingent Credit Line introduced by the IMF in April this year is a valuable tool in this regard, although we believe its design could be improved in certain respects.

6. This initiative, designed to prevent the contagion effects of international financial crises in countries that are following sound economic policies, is a major element in the new international financial architecture. Nevertheless, there is still no clear view in the markets as to whether a country's access to the Contingent Credit Line should be interpreted as insurance against risk, or, on the contrary, as a factor that increases the perception of risk and so adds to the country's cost of access to capital.

7. Mr. Chairman, I would now like to review some of the key proposals for strengthening the international financial system and expanding the scope and coverage of the initiative to reduce the debt burden of the heavily indebted poor countries . Strengthening of the links between debt relief and poverty reduction, in the context of the programs the IMF and the World Bank provide for their poorest and most indebted member countries, is of particular importance to several of our countries.

Strengthening the International Financial System

8. Given the globalization of international capital markets, it is difficult to imagine a system in which private operators would not play an important role not only in the prevention but also in the resolution of financial crises. Our countries support the initiative calling for voluntary participation by the private sector in the resolution of international financial crises, and in doing so wish to reiterate that it is necessary to exercise caution in designing and implementing the arrangements through which such participation would materialize. In our opinion, creditors should participate on a voluntary basis and in their own best interests; steps should be taken to minimize possible adverse effects on the risk premium applied to the developing countries; and the mechanism should be sufficiently flexible to accommodate the varying circumstances surrounding the issue of debt instruments by private entities.

9. In this process, the International Monetary Fund must help seek solutions that will be viable for both sides, and not impose any one specific solution on private creditors. The proposal by the industrial countries to incorporate provisions in bonds that would facilitate their restructuring is a positive initiative that should first be adopted in the developed countries, in both the public and private sectors, so as to establish a new

standard. Nevertheless, until conditions such as these prevail in the market, it is likely that this clause would adversely affect the access of developing countries to the international capital market.

10. The countries in our region approve of the efforts to strengthen the international financial system by going beyond the Basle standards. Nevertheless, the role to be assigned to risk assessment agencies must be approached with extreme caution, and care should be taken in general to ensure that the measures do not affect our countries' access to international markets, or the costs they incur in the process.

11. On the subject of choice of a particular exchange rate arrangement, our position is that countries are entitled to opt for whatever exchange system they consider best suited to their needs. The experience of our countries has demonstrated that the most important factor is the fit between the country's economic policies and the exchange system it has chosen.

12. There is general consensus that the process of capital account liberalization should follow an ordered sequence so as to minimize risks like those stemming from the contagion effect of crises originating outside the particular country. Our countries stand to benefit from the opening up of the capital account, as long as they follow sound macroeconomic policies and move ahead with essential structural reforms, including stronger financial system regulation and supervision. The Bretton Woods institutions should continue assisting those countries that require it to strengthen their public administration and the institutional framework through which such policies and reforms are implemented.

Linking the HIPC Initiative to Poverty Reduction

13. The countries in the region have consistently supported proposals for providing substantial debt relief for the heavily indebted poor countries. Consequently, we regard as very important the proposal submitted at the G-7 meeting in Cologne, calling for an increase in the scope and coverage of debt reduction for the HIPC countries; it is also essential, therefore, that the necessary financing be provided.

14. The countries in our region are making considerable efforts to contribute to this financing, not only through the multilateral institutions, but also in some cases by reducing the official debt of countries that have qualified for HIPC assistance – as Brazil has done. Some of the non-HIPC countries in the region should join in a plan to share the cost of such financing equitably.

15. In this connection, we wish to express our concern regarding the financial stability of the regional multilateral institutions, whose commitment to the HIPC Initiative could jeopardize their continuing role in financing development projects in the countries of the region. There is also some concern regarding the financial position of the World Bank and IDB, which are facing serious problems in financing their participation

in the enhanced debt relief framework. In our view, the main source of additional financing should be the bilateral contributions from the countries with the largest economic capacity, particularly those that took the lead in enhancing the HIPC Initiative.

16. The countries in our region applaud the IMF's efforts to find a creative solution to the problem of selling 14 million ounces of its gold reserves by employing a procedure that takes account of both the legitimate interests of gold-producing developing countries, and also the need to secure adequate resources to enable it to contribute to the enhanced HIPC Initiative.

17. The region welcomes the joint efforts of the International Monetary Fund and the World Bank to strengthen the links between debt relief and poverty reduction, in the context of the economic programs introduced under the HIPC Initiative. But we wish to emphasize that this is an instance of cooperation between two institutions with different mandates. The IMF should continue to concentrate its experience and expertise on issues relating to the macroeconomic stability of its member countries, while the World Bank should focus on development, including poverty reduction.

18. The countries in our region agree that it would be very difficult in practice to include specific social indicators in the quantitative and structural targets in Fund programs in general, although we acknowledge that, in HIPC countries, substantial progress on social issues and poverty reduction should form part of the final objectives of the Initiative.

The Peruvian Economy

19. Mr. Chairman, I would now like to refer to the economic situation in Peru. Fiscal stability and monetary prudence, combined with the ambitious program of structural reform that has been implemented over the present decade, have enabled Peru to reduce its inflation rate from 7,600 percent to the level of about 4 percent projected for this year. The stability thus achieved has created favorable conditions for sustained economic growth, spurred by private investment and exports. Over the last five years, annual GDP growth has averaged 6 percent.

20. This year, despite a continuing deterioration in the terms of trade and reduced capital inflows, we expect increases in output to reach 3 percent, with 5 percent in the year 2000. From 1993 to 1999, exports doubled, thanks to a sound macroeconomic base and maintenance of a floating exchange rate. The current account deficit has been narrowed, and this year it should be reduced by approximately 4 percent of GDP. It has been financed by the long-term private capital associated with investment projects resulting from the Government's commitment to macroeconomic stabilization and the adoption of measures to strengthen the existing legal framework, which is clearly favorable to domestic and foreign investment.

21. We have been able to deal with the adverse external events that have affected our economy since 1998, including El Niño, because of the soundness of the economy and maintenance of both a prudent level of international reserves and a strict framework of regulations and prudential supervision. It must be emphasized that the level of international reserves is more than enough to cover short-term debt and future external-debt maturities.
22. However, the shocks we have had to face have resulted in a slowdown in domestic demand and in tax collection. As part of the process of approving the budget for the year 2000, the Government has announced austerity measures to improve its fiscal position and foster the necessary conditions for the recovery of private-sector activity.
23. Peru's economic progress has brought about substantial advances in poverty reduction and improvements in the living standards of its people. I must emphasize how important it has been to win a victory over terrorism and finally establish peace with Ecuador. These events have been especially significant in improving the prospects for investors and, above all, in enhancing the welfare of our citizens.
24. Over the past decade, Peru's achievements have been substantial, consisting of economic stability, domestic and international peace, and integration into the global economy. We have established the basic conditions necessary for Peru's sustained growth over the coming years, providing opportunities for all its citizens within a market economy based on private investment, this being the foundation we are endeavoring to consolidate.
25. The great challenge of our time, and our principal national objective – the aim upon which a consensus must be reached by all social and productive sectors and all political groups, regardless of any ideological considerations or circumstantial disagreements – is poverty reduction, or, in other words, an increase in wealth through the creation of productive employment throughout the country. All our efforts are directed toward this basic goal, and should continue to be directed toward it, with increasing determination.
26. The challenges facing Peru are: to achieve growth which is first and foremost equitable; to develop a market-based economy; to strengthen democracy and institutions; and to guarantee access to health care and education for all. In Peru, we have taken up these challenges with the same earnestness and conviction that have characterized the country's performance over the past decade.
27. I wish to express the appreciation of the Peruvian Government for the efforts of the International Monetary Fund, and particularly the work of Mr. Michel Camdessus and the President of the World Bank, Mr. James Wolfensohn, and for the support that both institutions have provided for the economic and financial policies that the country has pursued since 1991. This year, Peru has signed a new three-year Extended Arrangement

with the IMF, a fact that confirms the county's commitment to macroeconomic stabilization, reaching beyond the approaching elections.

28. The approach of the new millennium, and these Annual Meetings of the International Monetary Fund and the World Bank, provide an appropriate time for us to renew our faith in a higher destiny for all the men and women on this planet. The 21st century will find Peruvians working and helping build a more humane and just world.

Thank you, Mr. Chairman

Washington, D.C., September 26, 1999