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INTERNATIONAL FINANCE CORPORATION
INTERNATIONAL DEVELOPMENT ASSOCIATION
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Statement by the Hon. **JAMES PETERSON**,
Temporary Alternate Governor of the Bank
and the Fund for **CANADA**,
at the Joint Annual Discussion

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Last year at this time, we were facing a very tenuous situation. You may recall that the *World Economic Outlook* document characterized the economic situation at the time as “unusually fragile”. Fortunately, for most of the world — though not all — the risks outlined in the document have not materialized. After the global financial turbulence of the past two years, and its devastating impact on economic activity and living standards in a wide range of countries, there are signs that the world economy is on the mend.

Economic Performance and Prospects in Canada

Developments in the Canadian economy have been more favourable than expected a year ago. In large measure, this reflects the government’s commitment to sound economic and financial policies -- low and stable inflation and balanced budgets or better.

Growth in Canada slowed significantly in the middle of 1998, owing in part to the global financial uncertainty and turmoil of the time. As the effects of this and other disturbances have passed, growth has strengthened, averaging an annual rate of 4.0 per cent over the last three quarters. As a result, the most recent consensus of private sector forecasters has real GDP growth upgraded to 3.5 per cent in 1999 and 2.6 per cent in 2000. The most recent International Monetary Fund Staff (IMF) projections are consistent with the private-sector consensus.

Policy Challenges

In part, this year’s more favourable global economic outlook reflects a number of policy steps taken over the past year, by both advanced and emerging market countries, to foster greater financial market stability and promote sustainable growth. Clearly, however, significant policy challenges remain.

Perhaps the most serious risk is that we do not succeed in implementing the necessary reforms to make our own financial systems and the international system less vulnerable to crisis. There are at least two reasons why our efforts could fall short. The first is complacency. We will be making a grave error if we let the return of relative calm in financial markets and the improvement in world growth prospects lead us to believe that further reforms are not necessary. The second danger is that we get caught up in a flurry of activity that, while giving the appearance of achievement, leaves critical issues or gaps unaddressed.

Although a lot has been started over the past two years, some fundamental questions remain about where we are going with reforms to the international financial architecture.

Consultative Fora

Asking the right questions is only one of the challenges. Another is to have the proper institutional infrastructure to deal with them. This is an area where we are making progress; for example, by giving a revitalized Interim Committee permanent standing as the International Monetary and Financial Committee and by creating the Financial Stability Forum.

Private Sector Involvement in Crisis Resolution

The workplans of the existing and new fora should be dictated by our vision of how we want to see the international financial system evolve. One of the key questions for us in this regard is how to ensure an adequate framework so that the private sector can be productively involved when a crisis does break out.

Canada believes that we need to develop mechanisms that enable an orderly workout of debts. The role of the official sector should essentially be that of a neutral broker, in the negotiation of a debt workout. The provision of large-scale official finance should be a rare occurrence.

To have the private sector involved in crisis prevention and resolution, however, we are going to have to establish a framework that will enable private investors to know in advance their responsibilities in the event of a crisis. And, we are going to have to ensure the mechanisms, which operate within this framework, balance the rights of creditors and the responsibilities of debtors to ensure that both sides have an incentive to achieve a cooperative solution with adequate financing supplied at an appropriate price.

Each crisis, however, will be unique. Each will have elements that we may not have encountered before. For this reason, we are going to have to be flexible and be ready to adjust to specific sets of circumstances.

Debt Relief and Poverty Reduction

So far I have devoted most of my remarks to problems and issues facing the international financial system. I would also like to address a few remarks to the equally important issues of debt relief and poverty reduction.

At the G-7 Summit this year, Canada pressed for faster and more generous debt relief for more countries and further action on poverty reduction. Canada fully endorses the two significant outcomes of the Summit in these areas. Debt relief under the new initiative will more than double. Combined with relief under current mechanisms and forgiveness of aid-related claims, this could release significant resources for poverty reduction programs.

Ensuring that the HIPC initiative is adequately financed is an important priority. While significant progress has been made to date in identifying financing, much more needs to be done. We would urge the international financial institutions to redouble their efforts to identify resources for this purpose. For its part, Canada will do its share and has fully paid in the \$40 million it committed to the HIPC Trust Fund and has also pledged some \$24 million from its refund on the IMF's Second Special Contingent Account (SCA-2).

Canada has also recognized the burden that new debt would represent for HIPC's and so, in addition to forgiving all its Official Development Assistance (ODA) loans from HIPCs, Canada now provides all its bilateral ODA on a grant-only basis. As well, Canada is committed to writing off 100 per cent of the commercial debt of the least developed nations. To prevent debt crises from becoming a recurring problem for developing countries, Canada also calls on lenders to adopt more transparent lending practices.

Canada's Export Development Corporation (EDC) has already taken steps to increase the transparency of its lending operations in developing countries, including making available a country by country breakdown of its loans. Canada calls on other creditors to join in developing common standards in this regard to help prevent future debt crises.

Expanding the HIPC Initiative by itself, however, will not be sufficient to meet the challenge of poverty reduction. The HIPC Initiative can only form one element of what must be a much broader attack on global poverty.

Collectively, we have a good sense of the key causes of poverty and where our efforts should be directed. In this regard, the education of women, in particular girls, is critically important, because educating women means educating families. This should form the cornerstone of our efforts in education — expanding opportunity to all segments of our societies.

We need to recognize as well that all too often families and individuals are poor because they are ill. Relatively modest investments in healthcare and pharmaceutical research targeted at the diseases of the poor could potentially yield enormous dividends.

In countries where governance is strong, a radical shift is needed in the culture of development. One that places the developing country – its government and its people – in the driver's seat. We are encouraged that steps in this direction are being taken by various players, with leadership emanating from the World Bank through its proposal for more holistic approach to development under a Comprehensive Development Framework (CDF).

However, the shift in development thinking must go further. Experience has shown that to be truly effective, development assistance needs to be targeted to countries whose governments pursue good policies and which are committed to developing and

maintaining strong institutions. Governance has been a dominant theme of development assistance work over the last few years and it must remain at the top of the policy agenda. In fact, good governance has become the essential building block for solid gains in poverty reduction and effective development assistance.

Effective multilateral institutions must also be a strong pillar of our development assistance efforts. We, as shareholders, have looked to the Bank to play a significant role in addressing the emerging markets financial crises over the last two years and we, therefore, have to acknowledge that this has created pressures on the institution. Canada remains open to supporting a capital increase for the IBRD as an option for reinforcing the institution's lending capacity. However, our support for this option would be predicated on a strong link between Bank lending and development effectiveness, as well as to performance on governance issues.

The Challenges for Small States

Canada views with particular concern the development challenges faced by the world's smallest states. We welcome the World Bank's joint involvement with the Commonwealth Secretariat as well as the IMF's commitment to further research and policy work to assist small states in a rapidly changing world environment.

Our constituent members in the Caribbean are clearly facing a difficult transition period with the changes to existing trade preferences, the decline in development assistance and the need for increased participation in the global economy.

These changes would be a formidable challenge for any developing economy. But for the small states of the Caribbean, many of which are at the mercy of potentially devastating hurricanes, these changes can appear overwhelming at times. Their vulnerability to a single event which can have disastrous economic and social effects magnifies the adjustment challenge they face. Small states have a vulnerability that large states do not have. External trade shocks and natural disasters can easily eliminate hard won gains in economic and social development. Their vulnerability is a fundamental differential that must be acknowledged.

Development, trade and finance institutions must recognize the impact of the phase-out of the Lomé preferences on small states and help smooth the transition. Financial and technical assistance, and time are needed in support of small state's efforts at restructuring their economies to the new external environment. Changes in global trade have made unsustainable some sectors that once accounted for a large portion of small states' gross domestic product.

The importance of this issue cannot be over-emphasized. The research conclusions and policy prescriptions laid out will be used by international development players to sharpen their interactions in small states over the years to come. Furthermore, and potentially most important, this research will set the stage for small-state participation and treatment within the next round of World Trade Organization (WTO)

trade negotiations. We look forward to seeing the results of this work by the time of the spring meetings next year.

Conclusion

Although the crises of the past two years have receded, we are still faced with important challenges. We must make headway while the waters are relatively calm, putting in place the conditions for a stable international financial system and improved living standards for all. Only then will we be able focus more on the opportunities that the world economy presents, and less on its challenges.