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Statement by the Hon. **MICHAEL CULLEN**,
Governor of the Fund for **NEW ZEALAND**,
at the Joint Annual Discussion

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Fellow governors and delegates, I am delighted to be able to participate in this meeting.

The international development co-operation architecture

We have seen a remarkable year in discussions on global development issues.

At the Financing for Development Conference in Monterrey, developed and developing countries reached an unprecedented agreement on the direction of our joint efforts to reduce poverty in line with the Millennium Development Goals.

Ministers and leaders agreed that development financing encompasses domestic and international finance, private funds and ODA, trade and investment, and that sound policy settings and good governance largely determine effectiveness.

Policy coherence is also vital, not only for developing countries so that efforts in one sector are not undone by conflicting policies elsewhere, but for donors too: rich countries which maintain billion-dollar agricultural subsidies and support undermine their assertions of commitment to developing country interests through aid and loans.

We look forward to rapid and thorough agricultural liberalisation for a true WTO "Development Round". New Zealand is committed to the developmental aspects of the Round. We wish to see that special and differential treatment provisions are used in the interests of growth and poverty elimination in developing countries. We will also continue to support trade-related capacity building for our developing country partners, through the Global Trust Fund, and through regional and bilateral assistance.

Taken together, Financing for Development, the Doha Development Agenda, and the recent World Summit for Sustainable Development outcomes, set us on the path towards a new era in development, and one in which the Bank and the Fund will have a key role to play.

We have however learned from experience and analysis, and agreed recently in Monterrey that common principles characterise effective development: strong country ownership, partnerships of mutual respect, good policy environments and governance, and targeting assistance to priorities which have the best chance of making progress towards the Millennium Development Goals (MDGs).

Nga Hoe Tuputupu-mai-tawhiti

I am pleased to announce that my Government established a new development agency in New Zealand on 1 July 2002, with a central focus on poverty elimination, to work with our key partners in the Pacific region and on the global stage to reach the ambitious targets the global community has set for 2015.

The new agency will face challenges, as will we all. Let me cite two as examples:

- Good practice suggests concentrating development assistance on what is effective, with a focus on results, and the necessary policy and institutional changes that need to be made to achieve this. But what if your key development partnerships are with states that may lack capacity, sometimes commitment to reform, and are beset by conflict, corruption, and vulnerability to natural disasters? A responsible partnership surely would assist overcoming these challenges, in the interests of helping achieve the MDGs, rather than ignoring their conditions in favour of support better performers elsewhere. We need to keep this firmly in mind in discussing effectiveness questions.

- Also, the development bargain struck at Monterrey and reinforced at Johannesburg involves improved governance and performance on the understanding that increases in ODA financing will follow. Is the donor community prepared to deliver? Are the performance indicators appropriate and realistic for measuring improved governance? We are, I suspect, some way from concluding positively on either count.

Debt relief

Governors, I would like briefly to address the ongoing issue of indebtedness.

In 1999, we committed ourselves to "deeper, broader and faster" debt relief to every eligible country that could translate the resources into better prospects for its poor. By the end of July 2002, agreements were in place—with relief flowing—to 26 countries, for debt service relief amounting to some US$27 billion.

Many factors contribute to poverty in developing countries: economic and political history, poor economic management, weak governance, armed conflict and such external factors as deteriorating terms of trade and climatic problems.

In about half of the 80 poorest countries, particularly the 41 HIPC countries, but in others too, such as in the Pacific, unsustainably high external debt has also become a key constraint on development.

We need to follow through on a comprehensive strategy to support achievement of the MDGs and reduce poverty, based on the twin pillars of home-grown efforts by all the

HIPCs to create the basis for sustained pro-poor growth, and on more decisive support from the international community.

The HIPC Initiative should be seen as part of this comprehensive approach. It is removing debt as a constraint to poor countries' struggle against poverty. It sets the stage for determined countries, supported by the international community, to overcome other constraints to exiting from poverty. Relief is delivered only to those countries that have demonstrated the commitment and capacity to use the resources effectively. In a world of scarce development resources, it is crucial to ensure that debt relief will actually make a difference in the lives of the poor.

As could be expected, the 12 countries yet to enter the HIPC Initiative face some of the biggest challenges to establishing a satisfactory track record, with many affected by conflict. It is, therefore, important that the international community presses forward with the HIPC initiative with pragmatism and commonsense, utilising the flexibility in the Initiative to enable these countries to progress to decision point quickly, where there is sufficient assurance that the additional resources will be used effectively to pursue poverty reduction. New Zealand also wishes to see countries make a robust exit from the Initiative, and so welcomes the use of realistic debt sustainability scenarios to assess post-HIPC debt sustainability.

Full creditor participation is also critical to the success of the Initiative. We strongly encourage all creditors yet to do so to confirm their commitment to the Initiative. We also encourage all shareholders of multilateral creditor institutions to play their part and ensure their institutions are able to participate fully.

Important as debt relief is, however, the gains to developing countries from trade liberalisation and from effective mobilizing of private capital flows would swamp those that accrue from debt relief. Further agricultural trade liberalisation is of particular importance to developing countries.

Global official development assistance in recent years has totalled US$50-60 billion a year. Debt relief under the HIPC Initiative was US$1.4 billion in 2001. At the same time, the current trade policies of some industrial countries directly neutralise the effectiveness of aid.

Greater coherence between aid and trade policies is essential. A coherent approach requires trade policies to create market opportunities for developing countries, and development policies enable them to respond to these opportunities. The trade and development communities must work together more closely than they have in the past. This is the essence of the Doha Development Agenda of the WTO, the Financing for Development Conference in Monterrey and WSSD. This is a significant challenge, and one that will require donor countries, development banks, the IMF, the OECD, WTO and UN system to engage with each other, as never before, and with their development partners. Achievement of the Millennium Development Goals rests on success in this.

Small States

New Zealand welcomes the growing commitment by the Bank and the Fund to addressing the unique challenges facing small states. Many challenges face our small state development partners in the Pacific—including vulnerability, isolation from markets, post-conflict trauma, and diverse social and cultural settings.

We look forward to increasing dialogue with the Bank, the Fund and our development partners on donor coordination and harmonisation in small states in the Pacific region.

As in any region, the Pacific has witnessed poor governance constraining development, as well as leading to conflict and breaches of fundamental rights of citizens. Small states face additional challenges of small populations and limited capacity in government – its functioning and basic machinery. One example of poor governance and systems failure is the emergence of gaps in banking supervision and regulation, tax evasion, and corruption. Pacific countries face redoubled challenges to meeting international standards and participating in initiatives to eliminate money laundering and the financing of terrorism, harmful tax, bribery and corruption, and improve financial and corporate governance. New Zealand, through its specialist agencies, Ministries and NZAID, stands ready to assist our neighbours to overcome these challenges.

The effectiveness of the IMF

The purpose of the IMF is to help ensure the orderly and stable growth of the world economy. New Zealand commends the reforms to date aimed at focusing the work of the Fund more sharply on core responsibilities and expertise. These reforms have included revisions to the IMF's financing facilities; a reassessment of the conditions attached to its loans; closer collaboration with the World Bank-in such areas as financial sector assessment programs, and debt and poverty reduction; a prioritisation of its technical assistance programs; and a firm commitment to transparency and accountability. At the same time, the effectiveness of the Fund will continue to be judged by it success in preventing and resolving crisis.

Surveillance is the main avenue to the Fund to identify an impending crisis early on. But crisis prediction will always be imperfect because crises are heterogeneous; they occur for different reasons in different settings and at different times. However, rather than being inevitable and pre-ordained, crises generally afflict countries that have entered a danger zone where the government lacks the political and economic capacity to fend off financial pressure.

New Zealand considers that it remains possible to identify steps to limit both the incidence and severity of crises, such as strengthening the supervision and regulation of financial institutions, rationalizing exchange rate regimes, and reforming fiscal and monetary institutions. Strengthening the focus and persuasiveness of Fund surveillance in these key areas is a priority.

A renewed bout of crises in emerging markets over the past two years should spur efforts to improve our framework for crisis resolution. Fund support in the wrong circumstances may encourage governments to cling to unsustainable policies. This permits financial vulnerabilities to build up, in turn leading to more severe fallout in crises. Repeated rescues also weaken market discipline, encourage more risky lending, and lead to an increase in vulnerability to future crises. At the same time, the costs of unsuccessful crisis resolution are high. Poverty increased much more in countries where crises led to defaults and financial collapse – Indonesia, Russia and Argentina – than in countries where international rescues helped restore financial confidence, including Mexico, Thailand, South Korea and Brazil in 1999.

The ultimate aim of IMF assistance is to create breathing room for a country to put its house in order. New Zealand welcomes the increasing recognition that IMF assistance is effective in reducing uncertainty and restoring investor confidence where there is a strong domestic constituency for reform. We strongly support the policies put in place to strengthen the basis for decisions in cases of exceptional access, including a more rigorous framework to ensure debt sustainability; and strengthening of the procedures and criteria surrounding exceptional access. However, the judgments in individual cases will remain very difficult and the ultimate test of these frameworks is whether our exceptional access programs are successful.

Where debt is not sustainable under a credible set of policies, the international community should recognize that restructuring a countries' debt burden is the only option to restore sustainability and growth. However, the option of restructuring debts is usually considered to be too messy, disruptive and painful and too threatening to the international system.

New Zealand welcomes the recent proposals to make sovereign debt restructuring less costly. A more orderly process could help to reduce the large economic dislocation associated with large scale debt restructuring. While we are willing to listen to proposals for reform, we must be realistic about the legal, political and bureaucratic challenges ahead.

No one should be under any illusion that the proposal for a sovereign debt restructuring mechanism (SDRM) would be easy to implement. First, proposals for a formal international mechanism for sovereign debt restructuring would imply a dramatic increase in the level of trust in international law and international institutions. Second, the criteria governing when a country's debts are unsustainable remain very uncertain. Third, a key impediment to proposals for reform of the framework for sovereign debt is the implications for the incentive for opportunistic sovereign defaults. A strengthened mechanism to ensure that debtor countries pursued sensible economic policies during the payment standstill would have to be developed.

The contractual approach offers a less intrusive solution to the problems of holdout creditors disrupting a restructuring agreed between a sovereign and a majority of creditors. We welcome the fact that the contractual alternative is being pursued in tandem with the work on the SDRM. Some have raised the possibility that contractual provisions will not work because they do not currently allow for voting across different bond issues. However, the key is not to make creditor litigation impossible but to make it sufficiently difficult so that restructuring is the most palatable alternative.

We look forward to further work on the appropriate design of contractual clauses. In terms of implementation, changes in listing requirements in key financial centres offers the quickest route to a contractual solution.

The 12th Quota Review

New Zealand acknowledges that there plausible case can be made either for or against a quota increase. We support addressing the large under-representation of several members of the Fund. Some say that perhaps the only way of addressing this under representation would be through a general quota increase, although our preference would be that the issue is dealt with immediately by other means. We must also acknowledge that there does not seem to be sufficient support for a quota increase, although there is always option to bring forward the 13th review should sufficient support develop.

Terrorist financing and anti-money laundering

New Zealand is committed to the fight against money laundering and terrorism, and its associated activities. We are well placed to meet the various obligations arising from international agreements and standards (including UNSCR 1373 and 1390 and the FATF 40+8 recommendations) and will be in full compliance with our international obligations with the enactment of existing or planned legislation.

It is important, however for the international community to be fully aware of the need for realistic expectations of, and assistance to, the various micro-states of the Pacific region and elsewhere if they are to play their part effectively. We should endeavour to avoid excessively prescriptive and complex approaches in the case of these micro-states, given their lack of infrastructure and limited resources.

Summary

Both the Fund and the Bank have made progress over the last year in making themselves more effective international institutions. A well-functioning Fund and Bank are important cogs in the global financial and development assistance architectures.

New Zealand commends the work of the leaderships and staffs of each institution in promoting global financial stability and reducing poverty in developing countries.