PRESENTATION OF THE FIFTY-SECOND ANNUAL REPORT

BY THE CHAIRMAN OF THE EXECUTIVE BOARD AND MANAGING DIRECTOR OF THE INTERNATIONAL MONETARY FUND[1]

Michel Camdessus

Mr. Chairman, Governors, ladies and gentlemen. I would like to join Jim Wolfensohn in welcoming you here and in expressing our thanks to the government of China and the people of Hong Kong for their warm, their generous, their splendid hospitality. What better opportunity could we have to see for ourselves the potential for Hong Kong to become an even more prosperous place, an even more dynamic center for the benefit of all of Southeast Asia within the framework of “one country, two systems”?

Mr. Chairman, our global environment this year is generally favorable. Indeed, many positive trends have been confirmed during the past 12 months. Global inflation remains subdued, and countries appear more committed to price stability than at any other time in the post-war era. Fiscal deficits are being reduced in many countries—a good omen for interest rates, investment, and financial stability. And exchange rates among the major currencies appear to be consistent with economic fundamentals. Thanks in large part to these strong fundamentals and continued progress on structural reform, the world economy grew by 4 percent last year, and is projected to expand by 4¼ percent this year and next. In fact, this trend could continue for several years to come.

We can also applaud further progress toward Economic and Monetary Union in Europe and signs of better policies and stronger growth in many developing and transition economies. Indeed, average growth in transition economies is likely to be significantly positive this year, for the first time during this decade.

But as favorable as the overall outlook is, we do not need to look very far to find problems that stand in the way of our objective, namely, high-quality growth. By this, I mean growth that is sustainable, that results in a permanent reduction in poverty and greater equality of economic opportunity, and that is respectful of the environment and the rich diversity of national cultures and traditions. What are some of these problems? In parts

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of Europe, malfunctioning labor markets; in parts of Asia and Latin America, but not exclusively there, fragile banking systems and persistent inequalities in economic opportunity. In all too many countries in the world, poor governance and inefficient use of public resources perpetuate poverty and impede human development. And we must not overlook the risk that inflation may pick up again in the economies where output is pressing upon capacity.

What we see in all these contrasting developments is a new globalized world economy continuously unfolding with new opportunities, new risks, and new requirements—all of them clearly illustrated by the recent turbulence in this part of the world. Let me focus my remarks on these global trends, beginning with these last events since they are so present in all of our minds.

Crisis in Southeast Asia

How did the events in Southeast Asia unfold as they did, against the background of more than a decade of outstanding economic performance?

Certainly, there were early signs of emerging macroeconomic problems, including a loss of external competitiveness. And these problems, in turn, exposed underlying weaknesses in the domestic economy, among them: a fragile and overexposed financial system, lagging industrial diversification, an inflated property market, and high levels of corporate debt. In our dialogue with the authorities over the past 18 months, we expressed our diagnosis, and we pressed for urgent measures.

Markets also expressed their disquiet. During 1996, the baht came under intermittent pressure. This year, the pressure increased, as doubts about the sustainability of policies grew. Finally, in the absence of a sufficiently comprehensive set of measures, the crisis broke. Meanwhile, the market's anxieties spread to other countries in the region.

I will say no more about the history of this crisis. Rather, let me put on record a tribute to Finance Minister Thanong and Governor Chaiyawat, who, confronted with a very deteriorated situation, had the courage to launch, in a very few weeks, a bold and comprehensive program that goes to the heart of market concerns about large external deficits and troubled financial institutions. Thanks to their efforts, the budget is moving back into surplus and a comprehensive restructuring of the financial sector is getting under way. Naturally, it will take time and forceful action by the authorities to restore market confidence. But I fully expect confidence to strengthen as the adjustment program is implemented.

In the meantime, the Philippines has taken necessary measures and extended its program with the IMF under which remarkable progress had already been achieved. Indonesia has substantially strengthened its policy stance in continuous dialogue with us. Malaysia is also adapting its already solid macro policies. In all of these countries, and in the supportive cultural context of strong Asian values, the authorities are relying increasingly on measures to strengthen economic fundamentals, rather than on controls. Hence, my confidence that markets will soon recover and that, after this period of adjustment, these economies will emerge stronger than before. If I had only one message to leave with you today, it would be this: these economies will emerge stronger.

What are we to make of these events? Well, we now have evidence that the IMF's procedures put in place after the Mexican crisis work, as they were expected to. In keeping with our efforts to strengthen surveillance, the staff's analysis of this region's problems was timely and on the mark. And once IMF assistance was requested, the Board's emergency procedures allowed a program to be put in place in record time. The Fund's assistance, in turn, catalyzed financial support from the region in an amount that, even by conservative estimates, is commensurate with the dimensions of the problem.

And yet, this crisis remains disturbing. Why? First, because the crisis was foreseen and preventable, but still struck with full force. Second, because one country's problems have not only cost its own economy dearly, but also, through contagion effects, imposed high costs on others. And more basically, because we all perceive the need to adapt further, in one way or another, to the new globalized context. This new context requires from each of us an even more acute, an even more far-reaching, sense of responsibility and solidarity. So, let us turn to what these entail.

Responsibility

Responsibility! Let me mention three aspects of it. First, vis-à-vis the market, responsibility involves maintaining the proper perspective about the benefits of private capital flows. Certainly, there are risks in tapping global markets: sometimes they react too late, and sometimes they overreact. No country—I repeat, no country—is immune to these risks. But let us not forget that markets also provide tremendous opportunities to accelerate growth and development, as Southeast Asia itself so vividly shows.

Thus, the lesson to be drawn from recent developments is not about the risks of globalization—and still less about demonizing the markets—but rather about the importance of exercising good citizenship when tapping them. Indeed, countries cannot compete for the blessings of the global capital markets and refuse their disciplines. Hence, the importance of pursuing sound policies that give markets confidence, of respecting the signals they provide, and of maintaining transparent and market-friendly policies so that they can do their job.

Second, vis-à-vis national policies, responsibility involves avoiding macroeconomic imbalances and correcting them when they arise. It also means making cost-effective use of public resources, explaining to citizens when and why policy changes are required, and taking the difficult steps to sustain growth in a timely manner. Constant refrain of the IMF? Of course! But may I suggest that it should also be the rallying cry of all those who value high-quality growth, particularly those who defend the poor. For indeed, it is the poor who are most likely to lose their livelihoods during economic downturns and who are least able to protect the real value of their incomes and savings during periods of high inflation. Thus, helping countries achieve monetary and macroeconomic stability—together with the necessary structural reforms—remains the IMF's major order of business.

The third aspect of national responsibility is to get policy priorities right. This is an obligation for each country in the world that benefits all of the others. Here in Asia it means that countries must give priority to the pressing business of strengthening current account positions and ensuring financial sector soundness, rather than to spurring growth prematurely.

In Europe, in its momentous journey toward EMU, it means giving at least as much attention to the urgent tasks of reforming social security systems and labor and product markets, as to the precise decimals around the fiscal consolidation targets.

Getting the priorities right also means that efforts to press on with macroeconomic adjustment must not delay other reforms that will enhance growth, that will make human development priority number one, and that will ensure that growth benefits are widely shared—this equity in the distribution of income on which Jim has so eloquently insisted. We know very well that achieving all of this requires not only macroeconomic stabilization, but also a range of broader reforms—a "second generation" of reform—to strengthen banking systems, allow labor markets to function better, create a more favorable climate for long-term investment, and level the playing field for private sector initiative. These reforms are not the icing on the cake, but essential ingredients in achieving sustained, high-quality growth. This is why the IMF has focused increasingly on a broader reform agenda, aspects of which may have caught your attention.

- You have heard that the IMF is now raising issues of income distribution in its ongoing dialogue with member countries and emphasizing the need for greater equality of economic opportunity. All true.
- You have heard that the IMF is speaking out more forcefully against unproductive spending, especially in countries with pressing social needs. And you have heard of instances in which members have decided to postpone military and other expenditures in favor of increased spending on education and health. All true.

- You have heard that the IMF has issued new guidelines on how it will deal with issues of governance and that, in some cases, our financial support has been interrupted or delayed due to concerns about corruption, accountability, and transparency. All true.
- You have heard that the IMF is helping its members increase the transparency of their economic policies and that we see this as a way to give policymakers more incentive to pursue sound policies, as a way to diminish opportunities for corruption, and as a way to make countries less vulnerable to the brutal reaction of markets when economic problems are eventually revealed, as they always are. Yes, all true.
- You have heard that, building on the work of the Basle Committee, the World Bank, and others, the Fund has developed a framework for financial sector stability, which will help the IMF disseminate a set of internationally recognized best practices in the financial area. All true.
- Finally, you may have noticed that, far from being discouraged by recent events in Southeast Asia, the IMF is all the more motivated to continue work on an amendment to the Articles of Agreement that will allow the Fund to promote freedom of capital movements. This, too, is all true.

Let me elaborate on this last point. I know you could ask us: “When you have such financial turbulence on your doorstep, is this the right time?” Yes, we believe it is!

Freedom has its risks. But are they greater than those of complex administrative rules and capricious changes in their design?

Freedom has its risks. But is there any more fertile field for development and prosperity?

Freedom has its risks! Let us go then for an orderly liberalization of capital movements. Certainly, the point is not to make a sacrifice on the altar of fashion. The point is not to encourage countries to remove capital controls prematurely, nor to prevent them from using capital controls on a temporary basis, when justified. Rather, the objective is to foster the smooth operation of international capital markets and encourage countries to remove controls in a way that supports the drive toward sustainable macroeconomic policies, strong monetary and financial sectors, and lasting liberalization.

In a nutshell, we are striving toward a multilateral and nondiscriminatory system that provides the necessary safeguards and proper transitional arrangements. The Fund would, of course, continue to exercise surveillance and stand ready to provide advice, technical assistance, and, when appropriate, financial support for countries’ adjustment efforts. We now have abundant evidence of the benefits of steady progress toward the freedom of capital movements and the prudence it requires. Let us now add this promising chapter to the work of our founding fathers. This certainly would have been part and parcel of their response to the challenges of today.

Responsibility is all of these things, including this cautious, but decisive, step toward liberalization. But responsibility must go hand-in-hand with solidarity.

Solidarity

What then are the requirements for international solidarity in this new global context?

Contagion effects can be so rapid, so overwhelming, so unfair to countries with sound policies that, no doubt, the first tenet of a charter for world solidarity is to "keep your house in order." The bigger the economy, the stronger the requirement. But no country is exempt from this responsibility to other countries. And no country should accept the risk of going down in history as one that triggered a domino effect.

But solidarity calls for more. There are many instances in which national efforts are likely to be more successful when bolstered with international support. And there are many challenges that exceed the capacity of individual countries to resolve alone. To cite one critical example, in spite of significant progress on economic reform, many of the poorest nations still do not attract enough foreign investment. For them, foreign aid is crucial.

I will not dwell today on what I have so frequently repeated about the responsibility of industrial countries to help minimize the social and cultural costs of integration into the global economy; to open their markets, especially to products in which the poorest countries have a comparative advantage; to prosecute their nationals for taking part in corrupt practices in foreign countries; to recognize that their ODA budgets are one of the best investments in building a more secure and prosperous world; to refrain from promoting unproductive military expenditure through aggressive sales strategies; and to provide the mutual assurances that obviate the need for wasteful military buildups. Let me only pay tribute here to the Latin American presidents who, in their *Declaracion de Asuncion,* reiterated their decision to keep their region free from arms races—a goal that would be advanced, of course, by increasing the transparency of military spending and, thus, enhancing mutual trust.

In this globalized world economy, solidarity also calls for countries to complement IMF surveillance by joining voluntarily with their neighbors in mutual surveillance on a regional basis. The idea is to develop a "club spirit" among neighbors through which they can encourage one another to pursue sound policies. Indeed, a healthy dose of peer pressure could be a most valuable contribution to stability.

Such a tradition is most firmly established in Europe, where regional surveillance and peer pressure have produced an impressive degree of macroeconomic convergence. The Group of Seven also practices mutual surveillance. In Asia, there are signs of growing regional cooperation—through regional groups and the region's rapid and sizable financial support for Thailand's adjustment program. This cooperation would be even more effective if it were supplemented with regional dialogue to ensure that the policies of individual countries are supportive of stable markets and high-quality growth throughout the region. To be effective, such regional surveillance has to be based on a sound analysis of the economic situation. The management and staff of the IMF are ready to contribute to regional surveillance to the best of their analytical and technical abilities. Supporting regional surveillance could be one of the important tasks of our Tokyo office, which we will inaugurate in December.

Of course, this suggestion does not detract from your responsibility to help the IMF discharge its ever growing, ever more complex central responsibilities. You know what this means, and you already do a lot by demonstrating on so many occasions your unfailing trust in our institution, by facilitating our surveillance work, and by reinforcing significantly the financial means available for us to discharge our systemic responsibilities.

The agreements on quotas and SDRs reached over the past few days demonstrate once again your tremendous confidence in and support for this institution. The membership has reached two critical decisions: one, to recommend an increase in IMF quotas by 45 percent, that is, nearly $90 billion; and, two, to recommend, through an amendment to the Articles of Agreement on which you will be voting this afternoon, a doubling of the amount of SDRs allocated so that all members can receive an equitable share of SDRs in relation to their quotas. Thanks to these agreements, along with the New Arrangements to Borrow, or NAB, that were agreed upon earlier this year, the Fund will be in a much stronger position to carry out its systemic role in this increasingly demanding global economy. We pledge to do our utmost to justify your confidence.

But there is another area where greater solidarity is needed. Of course, I mean Africa. You know how close to our hearts and minds this continent is. Earlier in this decade, sub-Saharan Africa was drifting toward the abyss of misery and marginalization after five consecutive years of negative per capita income growth. Now, thanks to the courage of leaders implementing adjustment and reform policies in the framework of ESAF-supported programs, this trend is being reversed, and the region is now in the third consecutive year of positive per capita growth. Indeed, average annual growth in sub-Saharan Africa reached 4½ percent last year and is expected to remain close to that level over the medium term.

Heavily indebted poor countries and the least developed countries performed still better. Each group recorded average growth of 5 percent last year, levels they, too, are expected to maintain over the medium term. However, we must do more and better. Not only is there a most pressing human problem at stake, there is also a systemic interest in preventing marginalization of the poorest and providing them with a powerful boost toward an early, safe, and full integration into the globalized economy. Thus, it is indispensable to have a level of ESAF resources that is commensurate with its essential, continuing role and the Fund's contribution to the HIPC Initiative.

Meanwhile, progress under the HIPC Initiative has continued, with about $1.5 billion committed for Bolivia, Burkina Faso, and Uganda. In addition, six other countries have been identified for debt reduction. We must support these efforts by finalizing the implementation of the compromise arrangement we adopted in September last year. I am certain that I can count on the support of all of you and on an extra bilateral effort before the end of this year to optimize the indispensable financing package.

Trust and financing are essential, but there is more that you can do to help us equip the world for its future. Let me mention only one challenge on the horizon: the evolution of the international monetary system into a tripolar system dominated by the dollar, the euro, and the yen. With macroeconomic policies within these currency blocs likely to be determined largely by domestic policy considerations, factors contributing to world exchange rate stability will have to be kept permanently under review—both for the sake of these three major currencies and to promote a satisfactory exchange rate environment for countries outside these blocs. Here we will need your support and your renewed commitment to the multilateral approach. A new reflection on the best ways to facilitate effective international policy cooperation is needed, along with a strong center for international surveillance, multilateral consultation, and monetary collaboration, a role that the IMF is mandated to fulfill by the very first words of Article I of its Articles of Agreement. We are still some way from achieving this last aspect of international solidarity. But it is a goal that has gained in importance and that the membership, together with the Fund, should now have high on its agenda.

During these few days in Hong Kong—this most exciting place—you have provided the Fund with a major new mandate and substantially strengthened its financial basis. You could not have given a more eloquent demonstration of your trust in the capacity of the Fund to serve the common good. Let me express my heartfelt thanks for that.

Since we move abroad every three years, in the year 2000 we will meet in Prague, the historic capital of the Czech Republic. By that time, we will have traveled farther on the promising paths of freedom, good governance, and solidarity. Surely we will have met the unexpected along the way, but you know that we will continue to do all that we can to be well equipped and not be caught off guard.

One thing of which I am pretty certain is that the country where we will be meeting—and a number of others between Vladivostok and Bratislava—will, by that time, be well advanced in their journeys toward modernity and cooperative, orderly market economies. With that, the Fund will have basically completed a very special task you entrusted to us. But new challenges will appear and, with them, new tasks: accompanying the countries of this part of the world from their "miracle times" to their maturity; supporting Africa as it builds on recent progress to achieve stronger, more sustainable, and higher quality growth; assisting many other countries in their "second generation" of reforms; adapting the international monetary system to the launching of the euro; and the list may be longer. We look forward to all these tasks with confidence. We know that the IMF can count on your support. We know that we will continue to join forces in making the most of the opportunities of our times.

Report to the Board of Governors of the International Monetary Fund by the Chairman of the Interim Committee of the Board of Governors on the International Monetary System

Philippe Maystadt

I am pleased to have this opportunity to report to the Governors, in my capacity as Chairman of the Interim Committee, on the work of the Committee during the past year, and on the significant steps that have been taken toward adding a new chapter to the Bretton Woods agreement.

The Decisions on SDRs and Quotas

At its meeting in Washington last April, the Committee requested the Fund's Executive Board to complete its work on the Eleventh Review of Quotas and on an amendment of the Articles to allow for a special one-time allocation of SDRs, and to report to the Committee at its Hong Kong meeting. On Sunday the Committee warmly welcomed the agreements reached by the Executive Board on these two important issues.

The Committee has recommended the adoption by the Board of Governors of the proposed Resolution on a one-time special allocation of SDRs at the 1997 Annual Meetings. The amendment will provide all members with an equitable share of cumulative SDR allocations, including those countries that have never received allocations of SDRs since they joined the Fund. It also will double the amount of allocated SDRs of 21.4 billion.

The importance of the agreement on the Eleventh General Review of Quotas must also be underlined. This agreement, which will result in an increase of 45 percent in total quotas and a distribution of quota shares that better reflects the relative strength of members' economies, will allow the Fund to consolidate its financial base relative to the size of the world economy and will also permit prompt and decisive action when needed. The recent market turbulence in Asia, and the Fund's response to it, supports the view that it is in the interest of the international community to have a financially strong Fund. To effect the agreed quota increase, the Committee has requested that the Executive Board submit a proposed Resolution for the approval of the Board of Governors before the end of this year.

Neither of these agreements would have been possible without the "spirit of compromise" that has prevailed among all members, from developing to industrial countries. Nor could they have been reached without the endless efforts of the Fund's Managing Director, who never lost faith in the merits of a new allocation of SDRs. Together with the agreement reached last spring on the New Arrangements to Borrow, the decisions on quotas and SDRs will place the Fund in a better position to fulfill its mission into the next century.

The "Hong Kong Statement" on the Liberalization of Capital Movements

At its spring meeting, the Committee agreed that the Fund has a central role to play in promoting the orderly liberalization of capital movements and agreed that the Fund's Articles of Agreement should be amended to give the Fund an explicit mandate and extend its jurisdiction to capital movements. The "Hong Kong Statement" adopted on Sunday provides the Executive Board and the staff of the Fund with the principles that should guide their future work on such amendment. Therefore, two points should be emphasized. The first is that freedom of capital movements is a desirable and worthy objective. In a global environment, it facilitates the flow of savings to their most effective uses and improves access to foreign capital, thus fostering growth and welfare. The second point is that, for these benefits to be realized, capital account liberalization should proceed in an orderly manner. Under the envisaged amendment, the Fund will have the task of assisting countries in making progress with the liberalization of capital movements at an appropriate pace, with adequate transitional arrangements and flexible approval policies.

A strengthening of the Fund's role along this path will help maximize the gains from liberalization and limit the risks associated with capital flows. This new mandate will contribute to the stability of the international financial system and the successful integration of member countries into the global economy.

Substantial progress has already been made by the Executive Board on designing the envisaged amendment. The matter is technical and complex, and the Committee requested the Executive Board to accord high priority to completing its work and submitting a report and a proposed draft amendment to the Board of Governors.

The World Economic Outlook and Lessons from the Recent Events in Asia

At its meeting on Sunday, September 21, 1997, the Committee noted the favorable outlook for the continued expansion of world output and trade, and set out in its Communiqué the reasons underlying this optimistic assessment as well as the range of potential risks and fragilities that will require vigilance.

The Communiqué also presents the Committee's conclusions on the implications and preliminary lessons from the recent developments in Asian financial markets. Three points should be emphasized. First, recent events have again underscored the importance for policymakers in all countries to ensure the internal consistency of macroeconomic policies, to strengthen financial systems, and to avoid excessive external deficits; rising capital flows may also require some adaptation of exchange arrangements to changing circumstances. Second, all members commended the Fund for its prompt and effective response to the events in Asia and welcomed the support provided by the region. Third, it was agreed to review the issues involved in the prevention of crises, particularly those related to strengthening the disclosure of information and to confidence building through openness and accountability. Moreover, the Committee requested the Executive Board to examine what further lessons could be drawn for the Fund's work and to report these findings to the Committee at its next meeting.

Strengthened Fund Surveillance

Much has been accomplished in the past year to strengthen Fund surveillance. In this context, the Committee welcomed the recent adoption of guidelines regarding governance issues in the work of the Fund as well as the ongoing efforts to enhance the soundness of financial systems, notably the establishment of core principles of effective banking supervision developed by the Basle Committee in conjunction with the supervisory authorities in a number of emerging market economies. It also noted that the transparency of the Fund's surveillance process has been enhanced through the recent introduction of press information notices on Article IV consultation discussions.

The HIPC Initiative

I would like to conclude my statement on the HIPC Initiative. The Committee welcomed the pace of its implementation. I am indeed pleased to report that between March and September 1997, the Executive Boards of the Fund and the Bank reached agreement on debt-relief packages for Bolivia, Burkina Faso, and Uganda, while preliminary discussions have been completed on the eligibility for assistance of Côte d'Ivoire, Guyana, and Mozambique. This means that real progress on debt relief is effectively under way.

Still, the Committee noted that, in light of the bilateral pledges received or in prospect, and the need to continue making commitments under the HIPC Initiative, further steps to secure the timely funding of this initiative would have to be considered soon. This will be required because the problem of unsustainable debt can be solved only if the HIPC Initiative's principle of achieving debt sustainability is matched by the willingness of all creditors to share equitably the burden of cost of the initiative. My hope is that the spirit of compromise and goodwill that has prevailed so far in Hong Kong will convince members who have not yet offered bilateral contributions to do so.

I want to conclude by expressing my satisfaction with the progress achieved during the past year, which will allow the Fund to help its members adapt to and benefit from the changes in the global economy.

REPORT TO THE BOARDS OF GOVERNORS OF THE BANK AND THE FUND BY THE CHAIRMAN OF THE JOINT MINISTERIAL COMMITTEE OF THE BOARDS OF GOVERNORS ON THE TRANSFER OF REAL RESOURCES TO DEVELOPING COUNTRIES (DEVELOPMENT COMMITTEE)

Driss Jettou

As Chairman of the Development Committee, I am pleased to report to you on the Committee's work over the past 12 months. I have, of course, only just become Chairman of the Committee. I am honored to have been selected by the Committee to succeed my predecessor as Finance Minister of Morocco, Mohamed Kabbaj. Minister Kabbaj served as Chairman for nearly three years, including at the April meeting this year. After the next meeting, the Chairmanship will rotate to another region.

My predecessor concentrated on three major points in his report last year. I believe these same three points deserve reemphasis on this occasion.

First, the Committee has been able to foster the close collaboration of the World Bank and the IMF on issues of importance to member governments. The HIPC Initiative gained its start in the Development Committee. It has been pursued with great vigor by Mr. Wolfensohn and Mr. Camdessus, and it has now become an established feature of international efforts to foster growth in the poorest, heavily indebted countries.

In April the Committee gave an additional encouragement to early implementation of the initiative. Yesterday we learned of major progress made by the Bank and the IMF Boards in starting six eligible very poor countries on the path of overall debt sustainability. While there are still funding issues to be confronted, the cooperation shown by the international community to make this common effort a success has been truly remarkable.

Yesterday, the Committee also broke new ground by discussing, for the first time, how to help countries combat corruption and improve governance. The Bank and the IMF have substantially expanded their attention to these issues. In doing so, they have joined with governments, international and regional organizations, and many nongovernmental organizations to confront these major impediments to development effectiveness, increased private sector activity, and economic growth. Our communiqué emphasizes that this is a global problem affecting all countries. The communiqué also reflects the broad support that now exists at the ministerial level for this more active role by the Bank and the IMF. Of even greater significance is the willingness of governments to accept the primary responsibility for ensuring that corrupt practices are reduced.

The Committee also discussed enhanced Bank and IMF collaboration in strengthening members' financial sectors. Recent developments have highlighted how important this subject is to our members. The opportunity for ministers, representing the entire membership, to review the issues informally with Mr. Camdessus and Mr. Wolfensohn was extremely valuable for all concerned.

The second point stressed by Chairman Kabbaj last year was the importance of improved procedures to the effective functioning of the Committee. The basic approach adopted last year has been followed again this year, with continued success.

The third point in last year's report was to note that the Committee has been able to focus its attention on a number of other key development issues as well.

In April the Committee heard from Minister Kaijuka of Uganda on the important subject of capacity building in Africa; yesterday we were honored by Vice Premier Zhu Rongji, who spoke on China's dynamic development experience.

The increasing importance of private sector development has been a central feature of the past two meetings. Yesterday, the Committee welcomed the World Bank Group's action program to encourage increased private participation in infrastructure. This initiative was proposed initially by a member of the Committee, Japan's Finance Minister. It has now become a focal point for strengthened Bank Group support for the private sector.

Moreover, the Committee has been seeking an early solution to the capital needs of the Multilateral Investment Guarantee Agency (MIGA). In this area there has been considerable progress. Yesterday ministers agreed on the components and timing of a $1 billion capital increase. This represents a major step forward. It will relieve MIGA's short-term financial constraints and provide it with a sustainable capital structure for the medium to long term.

The Committee has, of course, been concerned since its inception with the transfer of resources. The MIGA and infrastructure discussions have focused on how to enhance the effective use of private flows. Committee discussions of the Bank's Strategic Compact have reinforced Mr. Wolfensohn's efforts to strengthen the Bank's human and financial resources. Last spring, ministers had a good discussion of the World Bank's net income situation.

In April the Committee discussed how to strengthen support for development cooperation. This concerns the future of concessional flows for poor countries—including, of course, the International Development Association and the Enhanced Structural Adjustment Facility. This issue is intended as a building block for a possible future discussion in the Committee examining the prospects for multilateral concessional flows.

Next spring we will consider reports from the heads of the multilateral development banks (MDB) on implementation of the reforms proposed 18 months ago by the Development Committee's MDB Task Force.

The Development Committee is, I believe, playing an important role on behalf of the entire Bank and IMF membership. It provides a semiannual action-forcing event that spurs the institutions to act. It is a forum in which the members have an important opportunity to provide valuable advice to the institutions, and to one another, in a direct and timely fashion.

I will do everything I can to help continue the Committee to move in this direction.

Statement by the Governor of the Fund for Albania

Fatos Nano

First I would like to express my thanks for this opportunity to outline the new Albanian government's policy for the framework of the post-conflict rehabilitation that we have prepared in collaboration with specialists from the IMF and the World Bank. Both institutions have played a crucial role in Albania since 1992, and we place a high value on these ongoing contributions.

The tragic period through which our country has passed since the beginning of this year requires little comment from me. The sequence of events—from the collapse of the so-called pyramid investment schemes to the near anarchy that cost the lives of more than 1,500 people—is well known to you all. Our vision for the future of Albania commits us to look forward, while addressing the legacy of economic and social chaos that we inherited from the past.

The priority of the new government must be to complete the restoration of public order. This began with the arrival of the multinational forces participating in Operation Alba and is now being carried on by the country's security forces. At the same time, we are continuing the reestablishment and future development of democratic institutions, which we see as vital foundations for the stability of our emerging market economy.

An integral part of the restoration of law and order will be the ongoing reorganization of Albania's national police and security forces, as well as the appointment of appropriately qualified judicial authorities. The process of creating a professional, nonpartisan civil service—which we recognize will take time—has already commenced. In addition, Albania's parliament has already taken legislative steps to guarantee the freedom of the media by abrogating a controversial press law.

Turning to the macroeconomic sphere, the government's priority will be to achieve stabilization and to begin the process of bringing inflation—which reached 28 percent during the first half of 1997—under control. This will be achieved through a combination of sound macroeconomic policies and broader structural reforms. In support of these aims, we have prepared a program that includes immediate action to contain the country's fiscal deficit, place the remaining assets of the pyramid schemes under administrative control prior to an orderly liquidation, and press ahead with essential structural reforms, including the development of a well-regulated private sector banking system.

Following the implementation of this program, which will be supported by the IMF's six-month Emergency Assistance Program and by other multilateral and bilateral donors, it is our intention to move forward with a comprehensive strategy of economic adjustment and reform that will allow sustainable growth. Specifically, the new government will take such steps as may be necessary to maintain public order, while aiming to raise revenue collection from taxation and custom duties. At the same time we are committed to reducing all non-essential expenditure, supported by the Bank of Albania, which will maintain tight monetary and flexible exchange rate policies.

The Albanian government's fiscal policy will aim to impose strict limitations on the budget deficit, which will be less than 16 percent of GDP in 1997 and 12 percent next year, while ensuring that public order is maintained and a basic level of social security is provided for the most vulnerable segments of society. A critical factor in achieving these objectives will be external support for the budget, although steps will be taken to ensure that this does not add to inflationary pressure.

The government is also committed to increasing revenue through more efficient tax collection and by implementing a new package of revenue reforms. A central feature of this package will be an increase in the uniform rate of the value-added tax from 12.5 percent to 20 percent from October 1. Other measures will include increasing the excise duty on tobacco products and alcohol, raising the level of personal income taxes, and ending import tax exemptions by the end of this year. In addition, in order to avoid distortions of administered prices, the value-added tax will be added as a surcharge to these.

Domestically financed expenditure will also be reduced by a range of measures, including a reduction of 10–15 percent in the number of civil service employees by the end of 1998. However, it is planned to maintain spending on health and education at the levels already budgeted. Long-term reform will be supported by public expenditure review, which could be undertaken with the assistance of the World Bank.

External sector policies will focus on strengthening Albania's balance of payments position. It is anticipated that these will include increased receipts from exports and tourism, while a high priority will be given to encouraging foreign direct investment. The government is also fully committed to progressing toward accession to the World Trade Organization.

The government is strongly committed to the privatization of remaining state-owned enterprises. Those small and medium-sized enterprises still in state ownership will be privatized. A final cutoff date for the filing of restitution claims by previous owners or their heirs will be imposed.

Strategic investors will be actively sought for mining enterprises and utilities. We are aiming to bring the national telecommunications company, PTT, to the point of sale during 1998, while Albpetrol will also be prepared for privatization. The water and electricity industries will either be fully privatized or the services contracted out. A regulatory system will also be established for these industries.

I have today outlined the new government's program for immediate and near-term rehabilitation. While it is undeniable that the civil conflict earlier this year proved a severe setback to the country's economic, institutional, and social development, I believe that with the support of the international financial institutions and the wider donor community, Albania can make significant progress toward achieving economic and fiscal stability, leading to sustainable economic growth in the near future.

Statement by the Governor of the Fund for the Republic of Armenia

Armen R. Darbinian

I would like to express my gratitude to the Chinese and Hong Kong authorities for their outstanding efforts in mobilizing the Annual Meetings of the IMF and the World Bank. I wish them prosperity and success in the future implementation of the formula “one country, two systems.”

Armenia is a small country, with a well-known history and very impressive traditions, on which the newly created independent state was based. We announced political democracy, economic liberalization, and social safety as three main elements of our policy. Armenia was very successful in implementing its economic reform program, and the transition process in Armenia is known as a “success story” in both the Fund and the Bank. We took ambitious decisions on the privatization of land and state-owned enterprises, on price liberalization and macroeconomic developments aimed at inflation of less than 10 percent a year and at GDP growth above 6 percent, and on an increase in gross international reserves up to three months of imports. We have created a fully liberal regime for current account and capital account transactions. We strongly support the extension of the Fund’s mandate to capital account liberalization, because we strongly believe that there is a link between the country’s capital market on the one hand, and its macroeconomic stability and the solvency of its financial institutions on the other hand.

We strongly support the joint statement of the President of the World Bank and the Managing Director of the IMF on the institutions’ collaboration in strengthening financial systems, which is extremely important to ensure that emerging financial sector problems in all countries are promptly identified, as the more problems are recognized, the more non-emerging the markets will become.

And here Armenia with its short experience can also show an example of a “success story.” By implementing prudential regulations and the standards of the Basle Committee, we have developed high-quality supervision of the commercial banks by the central bank, which, in accordance with the newly created legislation, is strongly independent and has sole responsibility for conducting monetary policy and banking supervision. With these achievements in the supervision area, Armenia has become the leader of the Transcaucasus and Middle Asia regional group of banking supervisors under the auspices of the Basle Committee. We are very happy with the outstanding opportunity to share the experiences of each country involved in the activities of the group. In this regard we welcome the IMF and the World Bank’s increased attention to financial sector issues and their cooperation with the Basle Committee.

Through trade system liberalization and floating exchange rate regime implementation, we accepted Article VIII of the IMF Articles of Agreement, and we intend to improve our external position through the reduction of current account and overall balance of payments deficits. Armenia has pursued a liberal trade policy based on an open import regime with a low uniform import tariff and avoidance of quantitative restrictions on imports and exports.

We are currently applying for membership in the World Trade Organization, and we believe that we will be accepted at the beginning of 1998 and will again be among the first countries in transition to join.

We also welcome the World Bank's efforts in developing the regional cooperation, which in our case is becoming hopeful. Armenia's forced economic isolation has been significantly eased by the recovery of the Georgian economy and substantial volume of trade with Iran. We hope that our existing informal trade with our other neighbors, the Azerbaijan Republic and Turkey, will soon be turned into official commercial, trade, and financial transactions.

It goes without saying that our achievements are strictly connected with the cooperation developed with both the IMF and the World Bank. It refers not only to the substantial amount of financial assistance, but also to the outstanding efforts given by experts in the technical assistance area.

We were very successful in the implementation of programs under the Systemic Transformation Facility, the Stand-By Arrangement, and the Enhanced Structural Adjustment Facility with the IMF, supported by direct budget financing by the World Bank within the framework of Structural Adjustment and Rehabilitation Credits. Now, as we are predicting for the 1998 budget a substantial increase in our tax revenues by improving tax and customs administrations, we are very close to concluding that Armenia has already passed the rehabilitation part of the transition and has entered into the development era. In this particular context, we welcome the agreement on the quota increase and the IMF Executive Board's decision on a special SDR allocation that would effectively raise our ability to borrow for the development purposes. Of course, some clarifications in the quota calculation principles are needed, and we will work on this issue with the Fund staff.

We appreciate the World Bank Directors' decision to start IBRD lending to Armenia, which will accelerate and enhance the sustained economic growth achieved in past years and help the basically privatized economy to grow further. A number of major enterprises are being offered for privatization by the end of this year through international tender. We will continue the same policy next year of having an ambitious program of the infrastructure sector of the economy.

And here I would like to emphasize the importance of the International Finance Corporation and the Multilateral Investment Guarantee

Agency in providing support for investors and I encourage them to expand their activities in our country. I am sure that building upon Armenia's strong macroeconomic and structural reform record, these institutions could be more responsive to the country's pressing investment needs.

We appreciate the efforts of the World Bank Directors for the establishment of Development Grant Facility within the framework of the Institutional Development Fund. I think that these facilities could improve the real sector developments in newly independent states. We support Board discussions on the development of domestic capital markets and increasing privately financed infrastructure projects. I would like also to emphasize the ongoing importance of the Bank's remaining involved in public infrastructure projects, which are considered as priorities in Armenia.

As for the prospects for 1998, we considered our highly educated labor force to be one of the major factors contributing to the country's future economic growth. In this regard the government intends to make the reforms of the education and health sectors priorities in its overall economic reform program. As the domestic savings remain notably low, Armenia will continue to require substantial external capital flows.

In conclusion, I would like to assure you that Armenia will continue its strong reform performance, which, with the appropriate support of international financial institutions, will bring a sustainable economic growth and substantial improvements in the living standards of the people.

Statement by the Governor of the Bank and the Fund for Australia

Peter Costello

I thank the people and government of the Hong Kong Special Administrative Region for their warm and generous hospitality in hosting these meetings. This has been an historic year for Hong Kong. I am especially pleased that this year's Annual Meetings are being held here, at the heart of the most dynamic region in the world economy.

Asian Economic Growth

It is now widely recognized that the dynamism of the region over the past decade has been based on sound fundamentals:

- high savings financing high investment in people and infrastructure;
- a focus on exports and world trade; and
- good fiscal and macroeconomic settings.

A key factor in the recent turbulence in financial markets in the region has been concern over macroeconomic settings. Provided the fundamentals are restored and maintained, there is a sound basis for strong growth well into the future. Nevertheless, the recent experience underlines the point that good policy requires continuing effort. Good policy never takes a holiday. Sound financial systems are particularly important. Financial supervision must be flexible, so that it can respond to new challenges. As economies open to global financial markets in order to draw upon international capital flows, appropriate policy and prudential frameworks become more important, requiring more sophistication, more transparency, and more disclosure. This lesson is as relevant to developed countries as to the emerging market economies.

And when problems do emerge, we must be ready to respond. Australia was pleased to participate in the support arrangements recently put in place for Thailand. Our contribution to that package reflects our commitment to the region and the importance we attach to regional stability and growth. I would like to take this opportunity to thank the Fund for the key role that it played in assisting Thailand. We are confident that the IMF-supported program, fully implemented, will restore confidence and economic stability and reestablish a firm foundation for strong medium-term growth. We look to their authorities to advance its implementation.

The Fund and the multilateral development banks have an indispensable role to play in facilitating adjustment in member economies facing severe structural problems. This was evident in Latin America in the late 1970s and early 1980s, and more recently in Mexico and now in Thailand. The Fund could be assisted in this task by arrangements for enhanced regional consultation and cooperation between finance ministries and central banks. This could promote the early identification of problems and reinforce the willingness of countries to take necessary corrective actions at an early stage; it could also facilitate the speedy arrangement of financial support, as occurred in Thailand. We consider that furthering cooperation would be of assistance in the region.

Economic Policy in Australia

Many speakers at these meetings have spoken about the importance of sound macroeconomic policies and structural reforms for sustained growth and improved living standards. I am pleased to say that Australian economic policy is directed firmly at these objectives. Over the last 18 months, our government has introduced far-reaching economic reforms, which will reinforce Australia's strong and sustainable growth.

Monetary policy is now based on a compact with the central bank in which we have agreed to a target range for underlying inflation of 2–3 percent over the course of the cycle. Through the year to the June quarter of

1997, underlying inflation was only 1.7 percent, while for the 1997–98 financial year we expect it to remain at the bottom of the target range.

We are undertaking rapid fiscal consolidation and will have a budget surplus next year. That will be achieved without the proceeds from the privatization of government business enterprises, which will go to retire debt. Under current plans, commonwealth general government debt will fall from just under 20 percent of GDP in 1995–96 to close to 10 percent of GDP around the turn of the century.

We have been no less active in structural reforms. All aspects of regulation, at all levels of government, are being reviewed to ensure that they do not hinder competition and market mechanisms. I have announced a complete overhaul of the Australian financial system, including the establishment of a single prudential regulatory authority for all financial institutions. This recognizes the increasing integration of financial markets as the services and products of different institutions increasingly overlap and merge. I am also undertaking a major review of all aspects of corporate law to reduce unnecessary regulation and improve the economic focus of our corporate regulation. Australia is now at the leading edge of reform in these areas.

Mr. Camdessus, I applaud your call to the European countries to deal with unemployment through reform of their labor markets. Such reform is also essential in my country and is being pursued. Structural reform to the rigidities in the labor market is the answer to high structural unemployment.

There is no doubt that economic reform is difficult. The temptation to delay undertaking necessary changes that impose short-term costs is understandable. However, such responses can make the ultimate reform task larger and more difficult and thereby impose substantial long-term costs on the community.

Fund and Bank Activities

Over the past 12 months, we have seen considerable progress on several major initiatives involving the Fund and the Bank. The Initiative for Heavily Indebted Poor Countries has been implemented and is now operational. Agreement has been reached on the Eleventh General Review of Quotas and on a special allocation of SDRs. Moreover, the Development Committee agreed on September 22 to an increase in the capital of the Multilateral Investment Guarantee Agency. These are substantial achievements. The World Bank has also progressed in its broad reform agenda.

New Arrangements to Borrow

A particular achievement since last year's meeting is the agreement on the New Arrangements to Borrow (NAB) for the Fund. Australia is pleased to have played an active role in the negotiation of this new facility. I delivered Australia's adherence to the Managing Director when we met last Saturday and was pleased to chair the informal gathering of the group yesterday. I urge those countries that have not yet completed their processes for adherence to do so quickly, so that the NAB may come into operation at an early date. It will enhance the Fund's access to resources in a crisis and thus enable it to play a full role in handling such situations.

World Bank Reform

I welcome the progress that the Bank has made on its reform agenda. Six months ago, the Executive Board endorsed the Strategic Compact. Australia has been a strong advocate of reform in the Bank to improve its efficiency and effectiveness. Implementation of the Strategic Compact is an important step in this direction.

An organization responsible for promoting reform must lead by example in its own internal management. I congratulate the President for the great progress he has made on this front. He will have our support in doing what is necessary to ensure that this key area of the Compact remains firmly on track.

More generally, the various measures identified in last year's report by the Multilateral Development Bank Task Force need to be pursued actively, including coordinated efforts among the five banks to develop consistent evaluation standards. The World Bank has much to contribute to this process, but there is also much that it can learn from the experience of the other institutions. I look forward to the progress report from the five banks at the next Development Committee meeting.

We in Australia are very strong supporters of the Fund and the Bank. We are pleased with the leadership shown by Michel Camdessus and Jim Wolfensohn. We wish both institutions another successful year.

Statement by the Governor of the Bank for Austria

Wolfgang Ruttenstorfer

Europe's economy and economic policies have entered an important stage in two respects. First, economic wisdom strongly suggests that good economic fundamentals should translate into healthy growth. Second, the run-up to the third stage of monetary union has reached an important, albeit sensitive, point.

Inflation is slowing further from an already low level, and indicators of economic sentiment have recently reached a record level for the last seven years. However, growth is picking up less forcefully than inflation is coming down, and employment shows a disappointing performance, despite the fact that the European Union (EU) member states are taking steps to enhance the employability and skills of workers and the unemployed and to improve the functioning of labor markets.

The Austrian economy is broadly following the mainstream of European economic indicators. Trade-offs between these indicators, however, differ slightly compared with our European neighbors. In spite of lower-than-average GDP growth, unemployment is not increasing; however, there are no benign effects of sizable fiscal consolidation on interest rates. The latter phenomenon does not indicate a credibility problem for Austrian policy but points to an overall nominal interest rate floor represented by that of Germany, probably caused by the still diverging business cycles of the world's biggest industrial countries. Fortunately, exchange rates in the EU have recently adjusted themselves to equilibrium levels. Thus, in 1997 the competitive position of Austrian manufacturing has improved by some 5 percentage points compared with the level prevailing after the 1995 exchange rate turbulence in Europe. This gives us confidence for growing exports, a traditional prerequisite for an upswing in Austria.

Two factors make the current upswing less employment friendly than in the past. First, enterprises continue to invest in labor-saving technologies. Second, profits do not translate into domestic real investment to the degree that they previously did. The latter phenomenon has become more important in recent years, not only because of the growing internationalization of business, but also as a reaction to an unhealthy tax competition. We thus require a higher degree of international cooperation to overcome vicious downward spirals of tax competition.

At present, domestic policy priorities continue to center on further consolidating our public budgets, including reforms to maintain the viability of our public pension system in the long run; on solving labor market problems; on liberalizing energy and telecommunication sectors; and on encouraging the restructuring of our economy, especially capital markets, in the face of globalizing economic competition. While this policy mix successfully ensures that both budget consolidation and growth and employment targets can be balanced, it does not leave space for traditional expansionary policies. These issues highlight the need for our governments to also restructure the state as we know it today. To ensure its viability in the future, we will have to reduce activities across a certain range in order to focus on core activities.

Our consolidation strategy—amounting to savings of 4 percent from an implicit deficit of 7 percent, to less than 3 percent of GDP, which in 1996 was successfully implemented with a two-year budget—will be pursued further. In July 1997, the government decided on a budget package that covers two years, that is, 1998 and 1999. The early announcement of a consolidation of another 1 percent of GDP shows that the fulfillment of the Maastricht stability criteria is sustainable.

I am convinced that Austria will be in the first group of participants. This conviction is shared by the financial markets. The latter suggests a relatively large number of participants in European Economic and Monetary Union (EMU), despite the fact that meeting the fiscal criteria for a number of countries might still depend on the resurgence of growth this fall. Earlier concerns about a trade-off of price stability in the euro zone and the number of participants seem to have disappeared in light of the surprising convergence of inflation rates in Europe. Still, Austria's population needs to be convinced to take on the euro as a means of payment and as a store of wealth, despite its readiness to accept and undertake tough fiscal consolidation.

At the international level, the Fund for some time has been trying to find instruments to deal with the consequences of the increasing globalization of economies and financial markets. A whole new series of policy initiatives has been developed or can be considered as work in progress. Some of these policy responses, like the expanded supplemental lines of credit available to the IMF in the form of the New Arrangements to Borrow (NAB), have reached the stage of legislative approval in several countries. Austria will be among the NAB lenders and is likely to complete, this fall, the legal steps needed for its participation in this international financial safety scheme.

Other critical components of the Fund's policy response, like the Special Data Dissemination Standard to ensure timely and reliable provision of financial and economic information to the public, have been agreed to by the membership. Besides improving the availability and quality of data, the Fund's policy dialogue has become more transparent and open, as can be seen in the publication of its Article IV policy recommendations in the form of press information notices (the so-called PINs). The new emergency mechanisms established by the IMF following the Mexico crisis have been utilized while assisting Thailand and appear to have worked well.

Nonetheless, more needs to be done. The recent crisis in Southeast Asia's financial markets has underscored the critical importance of a sound financial system and the need for the Fund to pay more attention to financial sector issues that are capable of threatening macroeconomic stability.

Despite the strengthening of the Fund's surveillance role resulting from Mexican crisis-induced innovations in the Fund's policy instruments, the limitations of surveillance and the need for further improvements have become visible. It turns out that the information provided by member countries has been neither sufficiently comprehensive nor sufficiently reliable. Countries have ignored the Fund's warnings about problems with their balance of payments and financial sectors and have not heeded the policy recommendations of various organizations of the international financial community. The national and regional costs of such neglect have been high.

However, restricting capital movements is the wrong response to the financial turmoil in some emerging market economies. In my view, the declaration of the Interim Committee on the liberalization of capital movements under an amendment of the Articles of Agreement draws the right policy conclusions. While dealing with such problems of financial market crises as contagion effects and herd behavior, we need to recognize the growing importance of private capital flows for financing investment and growth in the world economy. It is necessary to maximize its benefits through an orderly process of capital account liberalization as envisaged in the planned amendment of the Articles, combined with policies promoting the development of sound financial systems. These, of course, are necessary but not sufficient conditions.

We welcome the recent agreement on the basic features of the Eleventh General Review of Quotas. This quota increase will permit both the strengthening of the Fund's resources and the correcting of the underrepresentation of some countries in terms of their quotas. It will thereby enable the Fund to continue to fulfill its mandate in the international monetary system. Like a number of other countries, Austria will receive a special quota increase that will help to narrow the imbalance between its relative position in the world economy and its capital share in the IMF. This is a step in the right direction, but further adjustment will need to be made in the future.

We welcome the consensus on amending the Articles of Agreement to permit a special one-time allocation of SDRs. This long overdue agreement will double the present amount of SDRs and equalize the SDR-to-quota ratio of all members at 29.3 percent. This will allow the transition countries in my constituency to fully participate in the Fund's SDR Department.

With regard to the heavily indebted poor countries, I should say that I am gratified that the first six cases of debt relief under the Initiative for Heavily Indebted Poor Countries (HIPC Initiative) have come to the Boards of the Bretton Woods institutions, thereby testing the practicality of the HIPC Initative approach. This success, together with the recent publication of the guidelines of the Bretton Woods institutions on governance—put in place to prevent misuse of public national and international funds and improve the management of public resources—breaks important new ground in development assistance.

The HIPC Initiative demonstrates how much satisfactory net income results are needed. Multilateral relief, with equitable contributions from all—also major—participants, needs to be supplemented by unilateral action. Therefore, Austria has decided—in an additional effort to its Paris Club contributions—to write off an amount of up to $130 million in outstanding loans to 11 mostly sub-Saharan countries. In addition to that, Austria contributes to the Multilateral Debt Fund for Uganda, and similar activities are planned for Mozambique. We welcome the fact that the World Bank and the IMF are doing their best to implement expeditiously the debt initiative, and we support the IBRD net income contribution.

While there are positive developments in these areas, the ongoing decline in bilateral official development finance puts an increased responsibility on the multilateral development banks. In this context, we welcome the World Bank's strategy to emphasize the role of the private sector in the development process and to support its stronger involvement. Providing financial and technical assistance to support this process will have an important leverage effect, thus supplementing or, wherever possible, even replacing traditional official development aid. Yet, as we know from our own experience, it is of great importance to set prudent framework conditions that guarantee satisfactory results for all stakeholders. The World Bank Group, with its outstanding and outreaching capacities, carries a major responsibility in this respect.

The high priority given to corruption and governance is crucial for economic and social development and also important in the context of stronger private sector involvement, where both the World Bank Group and the IMF play a major role in developing appropriate responses. The World Bank must, as a corollary, reinforce its support in capacity building and in establishing the necessary framework conditions in client countries. In our view, it is the Bank's responsibility to react appropriately if corruptive symptoms undermine its lending and nonlending activities. We are looking forward to the elaboration of operational rules and procedures in this respect, not least to safeguard the reputation of the Bank as an effective development institution.

Stronger involvement by the private sector in the development process will not render the World Bank superfluous. Even if clients' demand for loans is flat, and there is ample headroom, the Bank's income dynamics require a rethinking of its role and thus perhaps new strategies. We recognize that, at the same time, there are many interests and claims on the Bank's income and expenses and on its net income. To safeguard the effectiveness of the World Bank as the major multilateral financial institution in the long run, priorities will have to be set on the basis of profound analysis and discussions, which will not be an easy task. A number of strategies that are, in principle, sensible would entail major shifts in the Bank's role, structure, personnel composition, and income level and composition.

Finally, I am pleased to have signed the MIGA Convention in April 1997 on the occasion of my first attendance at a Development Committee meeting. The Austrian Instrument of Ratification was transmitted to the headquarters of the World Bank Group on September 10, 1997. The MIGA provides an extremely effective instrument for greater private sector involvement in the development process. The MIGA's capital constraints result not least from its successful work and the rapid expansion of its guarantee volume. This very positive development not only demonstrates the confidence of private investors in the economic development in borrowing countries, but also contributes to the relief of aid finance for the benefit of countries and projects that really need it.

It is our opinion that this positive development must not be hampered by capital constraints. We therefore support a quick solution for adapting MIGA's capital base to the demand for guarantees, and we are ready to contribute our share.

In concluding, let me say that the present global challenges are making themselves felt in each and every country. Those who are trying to actively manage this change will succeed. Those who merely attempt to stem the tide will fail. Looking at the Bretton Woods institutions, I am convinced that, although in different manners, they are at the forefront of those who are actively managing change and helping the tides of change to move forward in an orderly manner.

Statement by the Governor of the Fund for The Bahamas

William C. Allen

I have the honor to speak on behalf of the Caribbean Community and Common Market (CARICOM), namely, Antigua and Barbuda, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, Trinidad and Tobago, and my own country, The Bahamas.

I join my colleagues in expressing appreciation of the excellent arrangements made for these meetings by the Chinese government, especially to the people of the Special Administrative Region of Hong Kong. This beautiful city reflects the dedication and commitment of its people, whose achievements we admire.

We are pleased with the progress made on the Initiative for Heavily Indebted Poor Countries (HIPC Initiative) and fully endorse the proposals of the United Kingdom as spelled out in the Mauritius Mandate. Since March 1997, the Executive Boards of the Bank and the Fund have reviewed the eligibility of seven countries for relief, and decisions have been made in three cases. The Boards have also discussed preliminary HIPC documents for three other countries, and we are especially pleased to note that Guyana was included. We fully anticipate a favorable decision on our sister CARICOM state when this matter is formally considered.

We in the CARICOM are conscious of the responsibility of burden sharing. Almost all CARICOM countries have therefore indicated that they will contribute financing to the HIPC Initiative and the enlarged Enhanced Structural Adjustment Facility (ESAF). We hope, however, that developing countries that have provided debt relief under the Paris Club will not be called upon again to bear a disproportionate share of the burden, especially in situations where further concessions will be through a reduction in the foreign reserves of their central banks.

As for quotas and the SDR allocation, my fellow Governors from CARICOM welcome the agreement and hope that the formula for its distribution will not reduce the voting power of small states. We also welcome the agreement reached to provide all members with an equitable share of cumulative SDR allocations through a one-time special allocation of SDR 21.4 billion.

As regards an amendment of the Articles of Agreement, we are taking careful note of the ongoing upheaval in the economies and currency markets of Southeast Asian countries. There are valuable lessons for us in the Caribbean to learn from these events.

As you are aware, most of the CARICOM countries have fixed exchange rate regimes. We have argued that, given the openness and small size of our economies, and given that we are price takers for most exports, exchange rate stability is a key to maintaining low inflation and investor confidence. We are aware that this stability requires prudent fiscal and monetary policies and sound incomes policies. As a result of our adherence to such policies, most of the countries in CARICOM are enjoying relative exchange rate stability, without an erosion of external competitiveness. But, as experience in Southeast Asia shows, even with the most careful adherence to appropriate policies, few economies can withstand highly volatile capital flows.

The globalization of capital markets has been a reality for some time, and it is appropriate that the Fund should recognize and respond to this in a fundamental way. We are therefore prepared to support an amendment of the Articles of the IMF to make the promotion of capital account liberalization a “specific purpose” of the Fund, once such an amendment contains adequate safeguards that recognize the vulnerability of small open economies and that allow countries to take measures to protect themselves against destabilizing capital movements. In moving ahead, we also wish to stress that close and special attention be paid to the need for technical assistance for developing countries. We would not wish to move to capital account convertibility without paying due regard to the soundness of the banking system and to financial sector reforms in general. We should learn from experiences in Southeast Asia and from experience much closer to home. In this regard, we look forward to the Fund's review of financial liberalization in program countries.

We in CARICOM have, for a long time, been aware of the positive effect of good governance on economic growth, development, and improvement of the quality of life for our citizens. We therefore welcome the guidelines of the Bank and the Fund on governance and corruption, which are consistent with our commitment to good governance. Following them will help us protect and enhance our image for probity in business. This image is extremely valuable, given the importance of international business and financial services in a number of our economies.

The definition of governance is broad and includes transparency in government operations; promotion of an enabling environment for private sector activity, which requires a proper and adequate judicial system; and easily accessible, current, and high-quality economic information. Countries in our region intend to participate in the Fund's General Data Dissemination System (GDDS), but will continue for some time to require technical assistance with our data systems to reach the GDDS guidelines on quality, timeliness, and periodicity of our statistics. In addition, we welcome the publication of press information notices (PINs) and note that, since their introduction earlier this year, PINs have already been issued for Belize, Dominica, and St. Kitts and Nevis.

We fully support the Bank's effort to refocus its development agenda as set out in the Strategic Compact, and we are pleased with the success recorded so far. We are also aware that there could be some unexpected and undesirable outcomes as a result of the drive for budget savings. We hope, however, that the Bank will not be forced to curtail its activities in support of the Caribbean Group for Cooperation in Economic Development (CGCED); after the efforts by both the Bank and the region to expand the membership and improve the functioning of the CGCED, such action would be a setback.

As regards disbursement, the countries on whose behalf I speak have, for some time now, been making net repayments to the international financial institutions. This situation has its roots in the sometimes cumbersome and often time-consuming approval and disbursement procedures for investment lending and in the concentration on lending for adjustment in the previous decade.

We need to change this if we are to reverse the net flow of resources out of the region. We are prepared to work within the procurement guidelines, which have been modified from time to time to take account of special circumstances, but apparently this is not enough. Assistance with institution building to improve performance at all points of the project cycle—from identification through to appraisal and on to implementation —

will, in our view, become one of the most important aspects of our partnership with the Bank over the next five years or so. Perhaps the new investment instruments—such as the Learning and Innovation Loan and the Adaptable Program Loan developed by the Bank, which we heartily welcome—together with resources from the Institutional Development Fund, and participation in the human resource development effort by the Bank can be combined to identify and solve the problems that prevent speedy and effective implementation of projects.

We congratulate the International Finance Corporation on its program to become more active in the region. We will work together to ensure the success of its efforts.

As regards the World Trade Organization (WTO) and the Caribbean, in the Caribbean, the pursuit of stable macroeconomic conditions remains paramount, despite an increasingly difficult external environment, as protected markets for bananas and other traditional commodities are under challenge. This has been exacerbated in recent times by the adverse WTO ruling concerning bananas. The implementation of the WTO ruling will lead to the collapse of the banana industry, with disastrous economic and social consequences for the region, particularly the Windward Islands. The ruling also provides a shorter transition period than that which had been envisaged under Lomé. The industry has been implementing a restructuring program aimed at reduced costs and improved productivity that will require both time and assistance in combating the attendant external shocks.

To conclude, the challenge of expanding output while diversifying and liberalizing our economies from monocrop industries, mainly agriculture or tourism combined with a fast-growing labor force, is the key to long-run economic potential in the region. In this vein, efforts to restructure public sector management, state-owned enterprises, labor markets, and financial systems are being vigorously promoted and deserve the full support of the international community.

Statement by the Governor of the Bank for Bangladesh

Shah A.M.S. Kibria

It is an honor for me to address this august gathering today. First, let me thank the Bank and Fund authorities for organizing this meeting and the administration of Hong Kong for the excellent arrangements. It is appropriate that this meeting, the first international event of note to be held since the return of Hong Kong to China, should take place in Hong Kong, which, together with the neighboring regions of China, represents one of the world's most remarkable examples of accelerated investment and growth in the past few decades. There are many useful lessons to be learned here, as close economic relationships become closer, and as the transition leads to even broader global perspectives rather than a shift toward inward-looking economic strategies.

The structure of the world economy is going through a fundamental transformation, as many national economies are undergoing major structural changes and going through a process of rapid integration with the world economy. In a world that has accepted the primacy of market principles in economic management, the Bretton Woods institutions are called upon to play a crucial role in assisting the process of transition and integration while mitigating the disruptions that inevitably accompany such a major restructuring of economies.

Globalization and liberalization are the two defining characteristics of the current economic transformation. The two are very closely linked, as the successful liberalization of economies prepares them for the rigors of global competition and fully exploits that most powerful engine of prosperity, free trade. What has been most disconcerting for many countries, such as my own, has been the extent to which the difficult process of liberalization has not been supported by the hoped-for degree of globalization. As a consequence, our domestic industries have been subjected to intense competitive pressures, as anticipated, but the accompanying structural shift toward our export sectors has been slower than expected as we find that many external barriers to our export growth remain in place.

If we are all to reap the benefits of globalization and liberalization, it is essential to ensure a level playing field. The major international agencies must maintain an evenhanded approach in this regard, and must work toward the elimination of all trade barriers. Without such efforts, the relative latecomers to the international marketplace, which includes many developing countries and the economies in transition, will find that the adoption of liberalization policies and export-oriented economic strategies do not yield the expected results in terms of growth and development, and yet entail considerable adjustment costs and risks to macroeconomic stability.

The overall trend in flows of official development assistance (ODA) remains a source of concern. Despite the increased requirements of the economies in transition, the total pool of ODA resources has not expanded in real terms. This is sometimes argued to be of little concern, given the dramatic rises in private capital flows. This view ignores the reality of international capital markets, where lending concentrations often exceed the levels warranted by economic fundamentals. Low-income countries, excluding China and India, receive only 3.4 percent of total private capital flows to the developing countries, and the vast majority of developing countries receive very little private capital. For many countries the availability of ODA will remain a major determinant of their ability to undertake vital long-term public investments in social and economic infrastructure and in human capital. These investments are not only essential to ensuring a balanced and equitable pattern of growth; they also help to create an economic environment that can attract a larger share of the rising global flows of foreign financing and direct investment. Contrary to our expectation and need, the FY 1997 commitments of the International Development Association (IDA) declined by 33 percent to $4.6 billion from $6.9 billion, which indicates continued low disbursement in the coming years. Disbursement, however, was only marginally higher than the previous year.

The recent growth in private capital flows to developing countries has certainly been dramatic. In 1996 these flows exceeded $265 billion, which is about six times as large as the total at the beginning of the decade, and about five times the level of ODA. The surge in private capital movements presents important new opportunities for the developing countries willing to adapt to the new milieu. Clearly, maintaining stable macroeconomic conditions and a prudent stance of financial policies will be essential to attract significant levels of external private capital. This is particularly important for direct foreign investment, where resources must be committed for a considerable period of time.

With heightened capital mobility, the possibility of destabilizing speculation cannot be dismissed lightly. This is particularly true where short-term capital accounts for a large share of total private capital inflows. Wherever financial markets are thin and supervision and monitoring are weak, there is a danger that sharp movements in external private capital, which are not always driven by economic fundamentals, may pose serious risks to the economic stability of individual countries. Indeed, given the apparent "contagion" effects observed in the recent currency market turmoil in Southeast Asia, the problem can quickly assume systemic proportions. The inability of national or even regional initiatives to deal with such systemic problems have become increasingly apparent, but international efforts remain rather ad hoc in nature. The Bank and the Fund, which are already involved in advising governments as to how to deal with the pressures arising from the more integrated global markets, should play a more significant role in developing an effective international framework to deal with the problems stemming from volatile private international capital flows.

The present government of Bangladesh came to office just 15 months ago, following free and fair elections held under a neutral nonparty caretaker government. The elections were hailed all around the world as a major step toward establishing democratic rights and accountability in Bangladesh. Within a relatively short period, the government of Prime

Minister Sheikh Hasina has taken bold measures to enhance the quality of governance and to improve economic performance. Financial policies have been geared toward the maintenance of macroeconomic stability, while important steps have been taken to deal with structural weaknesses that have hampered the achievement of faster growth necessary to reduce poverty in Bangladesh. The budget deficit and external current account deficits as a percentage of GDP have narrowed, GDP growth has risen to 5.7 percent, while inflation remains moderate at an annual rate of less than 5 percent.

Important initiatives have been taken in a number of areas to support the government's economic strategy based on promoting export-oriented, private-sector led growth. These measures include the following reforms:

- opening up the infrastructure sector to private foreign investment. With the assistance of the World Bank, a Private Sector Infrastructure Development Fund has recently been set up to facilitate funding of such investments;
- establishing new energy plants under build-operate-transfer arrangements;
- revamping the bankruptcy laws to improve loan recovery and strengthen the banking sector;
- initiating reforms of the banking sector and the capital markets, with the support of the World Bank and the Asian Development Bank;
- accelerating the privatization of state enterprises, with the appointment of a private sector businessman to head the Privatization Board;
- undertaking extensive reforms of the legal system to modernize and speed up legal processes to support the expansion of private sector investment and commerce;
- setting up an Administrative Reforms Commission;
- passing legislation to set up effective local government institutions in line with a broader strategy of decentralization to improve service delivery and accountability; and
- strengthening parliamentary institutions by improving the committee system.

We believe that all these initiatives will help create the conditions and institutions for more efficient, transparent governance, and help promote the expansion of domestic and foreign investment and private economic activity in Bangladesh.

Finally, reforms are easy to talk about but difficult to implement. For a complex and difficult reform program to succeed, it is vital that a national consensus on basic issues is developed to support it. Reforms are associated with gains and losses to groups in each country and across countries, and may thus require compensation to those adversely affected by the adjustment process, except of course those losing rent-seeking opportunities based on distorted structures of trade and production. The process of consensus building and negotiation is a necessarily time-consuming process in a democratic system in which the government has no wish to ride roughshod over the will of the people. The Bank and the Fund need to remain sensitive to these issues in order to ensure the progress of structural reforms, and so should the industrial countries, the major contributors to the resources of these institutions.

Statement by the Governor of the Bank for Belgium

Philippe Maystadt

Over the past two years, considerable effort has been made to ensure that the IMF's activities truly reflect the process of economic globalization. Three examples will suffice:

- the establishment of a Special Data Dissemination Standard for member countries that have access or are seeking access to capital markets;
- the implementation of the New Arrangements to Borrow (NAB); the NAB is an important adjunct to the IMF's resources in the sense that it will help the Fund meet the special needs that countries face in global markets; and
- the establishment of a special procedure—the emergency financing mechanism—to give the IMF a rapid response capability in the event of serious financial crises.

The Three Historic Agreements Achieved in Hong Kong

However, the three major agreements reached in Hong Kong over the last few days—namely, the agreements on special drawing rights (SDRs), quotas, and liberalization of capital movements—are of equal importance for the IMF, IMF member countries, and the international financial system. In fact:

- the agreement with respect to SDRs is good news for countries in transition, which will now be able to obtain SDRs to which they had never before been entitled; moreover, the SDR agreement reaffirms the international community's commitment to maintain an international reserve asset that could prove highly beneficial in the event of a crisis within the international monetary system;

- the agreement on raising the IMF's quotas should increase the IMF's available capital by approximately $90 billion (BF 3,400 billion approximately); that is a truly substantial sum, which, while reflecting the growing power of markets, was also necessary if the IMF was to carry on performing its special role well into the next century;
- no less important is the agreement on an amendment of the Articles of Agreement of the IMF, which will enable the Fund to pursue the liberalization of capital movements. In fact, today's world is dominated less by flows of goods and services than by flows of capital. The IMF should therefore be equipped with the legal authority it needs in order to provide IMF members, to a greater extent than in the past, with sound advice on capital account liberalization and to engage in constructive dialogue with member countries in a way that reflects the contrasting circumstances encountered within each country.

There are two additional reasons why we support the principle of an amendment.

First, with its new mandate, the IMF may be expected to devote further resources to studying capital movements in order to enhance the credibility of its recommendations by ensuring that the latter are predicated upon the Fund's capacity to explain and anticipate the numerous factors involved in the functioning of financial markets. This mastery of the subject—which the Fund must still acquire—will in turn allow the organization to enhance its stature, strengthen its surveillance of capital movements, and thus help maximize the benefits and minimize the risks of capital account liberalization.

Second, by allowing sovereignty over capital account restrictions to be transferred from member countries to the IMF, the amendment of the Fund agreement will strengthen the authority of what is, after all, a global institution within an area in which member countries had for practical purposes given up a good deal of their sovereignty already. This is a step in the right direction, because one way of responding to the risks of globalization is to treat official institutions accordingly, in other words, to give them a global dimension. Our goal should be to have official international institutions that are equipped to pursue the adoption and implementation of globalized strategies whenever it becomes clear, according to the principle of subsidiarity, that only global solutions will suffice to deal with such problems effectively.

One cannot overstate the importance of the challenges involved. That is why the authorities of member countries—including those responsible for supervising and regulating financial markets, such as the *Commission bancaire et financière* in Belgium—should seek to explore the full range of consequences liable to result from the envisaged amendment, and if necessary, to propose appropriate measures to address the various practical issues still unresolved. It is also incumbent upon the IMF to launch a campaign of education and outreach so that, in the wake of the consensus achieved within the Interim Committee, a similar consensus can be forged among all parties affected by the agreement, including the private sector.

I would now like to touch upon three issues that I am confident will continue to figure prominently in the activities of the Bretton Woods institutions; I am referring to the work performed by the IMF and the World Bank in the developing countries, the HIPC Initiative, and the introduction of the euro.

Requirements for Achieving Meaningful Poverty Reduction

The challenges of development are as immense as ever, hence, the need for ongoing efforts to identify ways to enhance the effectiveness of IMF and World Bank operations. It is with these thoughts in mind that I would like to make a couple of observations.

- First, I believe that growth cannot be sustained over the long term unless it is based on promoting private sector activity; this is essential if economies are to have the flexibility and dynamism they need in order to become fully integrated into the global economy. From this perspective, the Bretton Woods institutions still have much work to do if they are to stimulate foreign direct investment in the countries of sub-Saharan Africa, which continues to languish at about $2 billion a year (compared with a figure of $100 billion for all developing countries in 1997). I therefore welcome the renewed efforts of the International Finance Corporation (IFC) to give more support to the private sector in African countries. In light of the improving prospects for the countries of sub-Saharan Africa, it should be possible for the IFC to approve a larger number of projects than in 1996 (only 26).
- Second, we must make more of an effort to ensure that both the authorities and the general public in the countries concerned can gain a clearer understanding of the general philosophy underlying the adjustment and reform policies recommended by the World Bank and the IMF. That is particularly true of the IMF; Mr. Camdessus, you will forgive me for expressing my opinion so candidly in this matter. Such efforts are essential if we are to garner maximum sup-

port from local populations, for in the absence of such support, adjustment policies have scant prospect of success over the long term. Undoubtedly, the guidelines recently adopted by the management and Executive Boards of the Bank and Fund, as well as by the Interim Committee, should be most helpful in facilitating dialogue with the countries concerned and forging a broad-based consensus around the required reforms. For example, I would emphasize the focus on maintaining social cohesion, respect for the rule of law, and human resource development that is a notable feature of the Interim Committee Declaration on Partnership for Sustainable Global Growth. However, in order to succeed, the new guidelines adopted “at the top of the pyramid”—if I might be permitted the expression—must also become institutionalized at all levels of the Fund and the Bank.

Belgium’s Support for the Initiative for Heavily Indebted Poor Countries (HIPC Initiative)

I would now like to discuss the HIPC Initiative.

Encouraging progress has been achieved since the HIPC Initiative was adopted one year ago. Firm decisions have already been taken with respect to Bolivia, Burkina Faso, and Uganda, and three other countries are expected to follow suit; namely, Côte d’Ivoire, Guyana, and Mozambique. I share Chancellor Brown’s view that all eligible countries should be able to join the initiative by the year 2000, because, of course, the initiative is open to all heavily indebted poor countries that are prepared to adopt or implement a reform and adjustment program supported by the IMF and World Bank.

This means that all creditors that have committed themselves to contributing to the funding for the initiative should reaffirm their commitment by providing the necessary resources in a timely fashion.

Rest assured that if last year’s agreement were not followed through, it would become very difficult for the Bretton Woods institutions to launch any future initiatives entailing the use of substantial resources. In fact, no agreement on such initiatives will be possible unless everyone is convinced that all member countries will participate on the basis of their capacity to contribute, in the spirit of cooperation and partnership that multilateral institutions will have to demonstrate if they are to face the challenges of the future.

It is with such thoughts in mind that I shall propose a twofold contribution from Belgium for the funding of the HIPC Initiative:

- I shall first propose a contribution of SDR 44 million (i.e., approximately Belgian francs 2.2 billion), through the continued holding of the National Bank of Belgium's existing deposits held with the IMF, and through the recycling of Belgium's reserves in the Special Contingent Account 2; this amount corresponds to 3.4 percent of the required total bilateral contributions (SDR 1.3 billion); this percentage corresponds to Belgium's share in the total quotas of the industrial countries.

- I then propose that Belgium make a contribution in 1998 to the HIPC Trust Fund, created by the World Bank to serve indebted poor countries; I will ask for this contribution to be earmarked for the African Development Bank (ADB) in order to help the ADB to participate in the initiative.

The Required Reforms in the Wake of a New Currency: The Euro

In conclusion, I would like to offer some observations on the subject of European Economic and Monetary Union (EMU) and the establishment of the euro on January 1, 1999.

Recent doubts as to whether the euro project might have to be shelved, as encountered in last year's discussions, have been dispelled.

However, there are those who still question whether the introduction of the euro will bring about any fundamental changes in international economic relations, primarily because the insider countries are supposed to retain a good deal of autonomy in the conduct of their economic policies.

To all those who would downplay the importance of the euro, let me say that I am firmly convinced of the following:

- the introduction of the euro bids fair to become a watershed event in monetary history, the most important of its kind since the abolition of the Bretton Woods system of fixed parities;
- the advent of the euro will have an impact on the structure of international monetary relations, particularly with respect to the Group of Seven and the IMF itself;
- with its emergence as an international reserve currency, the euro will become a key focal point for a number of countries, and this, I am convinced, will ultimately promote further debate on the changes needed in the machinery of the international financial system.

Under the circumstances, I believe that we should move expeditiously to prepare the remaining European and international decisions required to lay the full groundwork for the introduction of the euro in view of its consequences at the internal and external level.

It is clear that these consequences will be largely dependent on the economic policies pursued within the euro zone and on the relative efficiency with which such policies are coordinated. This is true for the participating countries, but it is also true for the rest of the world—albeit to a lesser degree—inasmuch as the economic policies coordinated within the EMU framework are bound to have an impact on non-EMU countries. In this way, the implementation of the EMU may make the international monetary system more symmetrical, thereby ensuring that the benefits expected to result from the cooperation among the various "poles" can be more uniformly distributed.

As indicated recently by Governor Verplaetse, a decisive factor will be the EMU's capacity to define a "policy mix" capable of ensuring internal stability while passing muster at the international level.

There is no reason to doubt the anti-inflationary resolve of the future European Central Bank (ECB). Indeed, I am convinced that the ECB will move swiftly to establish its credentials in this matter and to underscore its focus on price stability.

Fiscal policy will remain the prerogative of member states, even though they have accepted a common framework pursuant to the Stability Pact, designed to ensure the maintenance of fiscal discipline. Accordingly, the recent efforts to bring down public deficits will not have been wasted.

It follows that the EMU policy mix may represent a significant departure from times past, when a comparatively strict monetary policy was supposed to compensate for the deficiencies of fiscal and/or wage policies. A more balanced policy mix ought to contribute toward enhancing the outlook for growth within the European economy.

For all of these reasons, I am convinced that the euro will be an intrinsically sound and stable currency. However, the exchange rate for the new currency will not be determined solely by the policy mix within the euro zone itself; it will also depend on its position vis-à-vis that of its major partners. Economic policies in the United States and Japan will obviously continue to be important for the overall economic system, highlighting the advisability of the tripolar cooperation that Mr. Camdessus mentioned yesterday at the end of his statement.

Statement by the Governor of the Fund for Bosnia and Herzegovina

Monojlo Coric

According to the Dayton Agreement, Bosnia and Herzegovina is within its internationally recognized borders. It consists of two entities—the Federation of Bosnia and Herzegovina and the Republika Srpska. For the time being, the Council of Ministers of Bosnia and Herzegovina has very limited authority. Its composition is nationally balanced, ensuring the equity of all nations from Bosnia and Herzegovina.

The state institutions of Bosnia and Herzegovina are in charge of the following fundamental economic responsibilities: monetary policy is carried out by the central bank, which was established on August 11, 1997 and acts as the currency board, and is responsible for foreign debt management and payment, and foreign trade and customs policy. Other economic functions are mainly under the purview of the two entities.

It is very important that a stable peace has been sustained during the past 21 months. This has created the basic premise for the September elections held last year, as well as for the local elections held 10 days ago, by means of which we finalized the process of establishing the democratic institutions at all levels of authority.

Despite some obstacles and delays, the institutions of Bosnia and Herzegovina have become operational; namely, these are the presidency of Bosnia and Herzegovina, the Parliamentary Assembly of Bosnia and Herzegovina, the Council of Ministers, and the recently established central bank.

In June 1997, a package of laws was adopted, among which the most important ones are the law on the central bank of Bosnia and Herzegovina, the law on the budget of Bosnia and Herzegovina, and laws on foreign trade, customs tariffs, and external debt.

Industrial production, market supply of goods, stabilized prices, salaries, and other indicators of economic progress in the Federation of Bosnia and Herzegovina point to constant improvement, and certain progress—although to a lesser extent—has been registered in the Republika Srpska. It is estimated that the GDP rate in 1996 was 50 percent, but owing to the slow inflow of international assistance, this increase in GDP will be much lower in 1997.

Immediately after signing the Dayton Agreement, Bosnia and Herzegovina became a member of the IMF, and it later became a member of both the World Bank and the European Bank for Reconstruction and Development. The economy has been devastated by the war, which has practically ruined the import capacity of the country. From a country that had a continuity in payment surplus before the war, Bosnia and Herzegovina has become a country with very high deficits on its current accounts. These deficits are mainly covered by the donations of the international community. Donors assistance has been mobilized to meet the needs of reconstruction, with three donor conferences organized by the World Bank and the European Union held in December 1995, March 1996, and July 1997, respectively.

A total program for the period of three to four years amounts to \$5.1 billion. We received promises for 1996 in the amount of \$1.8 billion, but as of now only two-thirds of the commitments have been realized. The Donors Conference for 1997 was held with a delay—we expected commitments in the amount of $1.4 billion, but the amount finally promised was $1.1 billion. Bosnia and Herzegovina expects that the promises from 1996 will continue to be implemented and that the commitments for this year will begin to be realized.

The World Bank stands as a very efficient partner of Bosnia and Herzegovina, both in providing technical assistance, organization, and mobilization of assistance from a large group of international donors and in approving a number of programs for reconstruction (18 programs) that have been successfully realized on the field. These programs cover almost all sectors—the economy, infrastructure, education, health, housing, and pensions—and include support for macroeconomic policy reforms.

Bosnia and Herzegovina has taken part of the former Yugoslavia's external debt to international financial institutions, and it has started to service this debt regularly. Both entities have carried out a solid fiscal policy. The entities finance public expenditures by relying on the collection of their own revenues and trying to avoid borrowing of the domestic sector. It is very important to pay attention to constantly increasing these revenues, which results from an increase in economic activities and more efficient work on the part of tax and customs administration. These revenues are not enough to fully finance extreme needs, especially those in the social sector.

For three years, monetary policy has been carried out by applying the currency board arrangement or by using foreign currencies. Monetary institutions have mainly avoided credit to the banking and private sector. An increase in money during this period has been based on the inflow of foreign exchange currencies, either from the current inflows or from international assistance.

The creation and work of the Central Bank of Bosnia and Herzegovina have been an important success. The Parliamentary Assembly of Bosnia and Herzegovina adopted the Central Bank of Bosnia and Herzegovina Law on June 20. That law establishes the functions and governance architecture of the Central Bank of Bosnia and Herzegovina.

The central bank is responsible for issuing the currency and monetary policy in Bosnia and Herzegovina. The central bank's discretion in policymaking is very limited for the first six years, as it will operate as a currency board; that is, domestic money (the konvertibilna marka) can only be issued in exchange for foreign exchange—in practice, the deutsche mark.

A corollary to this statement is that the central bank cannot grant credit to anyone. This is a desirable feature for three reasons.

- It guarantees that inflationary monetary expansion will not occur again.

- It avoids the frequent need for politically sensitive decisions on monetary management.
- It strengthens the credibility of the new institution and supports public confidence in the new domestic currency.

The governance structure of the central bank involves, at the top, the Governing Board, which is in charge of board policymaking decisions but without executive responsibilities. The Governing Board is headed by the Governor—during the first six years, a foreigner appointed by the IMF in consultation with the presidency of Bosnia and Herzegovina. The Dayton Accord spells out these details as well as others concerning the voting procedures within the Governing Board. The Governor is also the Chief Executive Officer, and in this capacity he is aided by three Vice-Governors appointed by the Governing Board. Internal controls are carried out by a General Comptroller and three Deputy Comptrollers similarly appointed by the Governing Board. The operations of the central bank are to be carried out by a head office, which is located in Sarajevo and Pale, and by main units of the central bank located in Sarajevo, Mostar, and Pale. The Head Office consists of the Office of the Governor, the Office of the Comptroller General, and three functional departments—banking services, administration and finance services, and research. These departments perform a coordination role with respect to the activities of the three main units. They also carry out some decentralized functions, such as executing the directives of the Governing Board with reference to the investment of foreign reserves, or provide statistical analyses of economic data and balance of payment projections.

Without getting into too much detail, the general picture is that the Central Bank of Bosnia and Herzegovina has a decentralized approach to discharging its functions. This strategy is both workable and realistic in light of the current situation in Bosnia and Herzegovina.

Of course, the Central Bank of Bosnia and Herzegovina has jurisdiction only in konvertibilna marka transactions, for example it sets—remunerated—reserve requirements against konvertibilna marka deposits in the banking system. Other foreign currencies continue to be used in Bosnia and Herzegovina, although the presidency of Bosnia and Herzegovina and the governments of the two entities—the Federation of Bosnia and Herzegovina and the Republika Srpska—will take active steps to encourage the use of konvertibilna marka, for example, in the state and entity budgets.

Unlike other central banks, the Central Bank of Bosnia and Herzegovina is not directly involved in banking supervision, which is the responsibility of the entity-level banking agencies. The Central Bank of Bosnia and Herzegovina Law does, however, call for a coordination role of the central bank to ensure a harmonized supervision framework throughout Bosnia and Herzegovina.

The Central Bank of Bosnia and Herzegovina stands ready to convert on demand konvertibilna marka for the deutsche mark, and vice versa, at a one-for-one fixed rate. Thus, the exchange rate regime of Bosnia and Herzegovina is completely liberal: there is guaranteed, unrestricted convertibility of the konvertibilna marka for both current account (which equals exports, imports, transfers, and interest payments) and capital account (which equals foreign investment and debt-servicing) transactions.

The Central Bank of Bosnia and Herzegovina started operations on a limited scale on August 11, 1997, as required by the law. In this initial phase, the Central Bank of Bosnia and Herzegovina has taken over from the previous central bank, the National Bank of Bosnia and Herzegovina all—and only—the monetary liabilities that the law allowed it to take over, namely, Bosnian dinars in circulation and deposits of commercial banks at the National Bank of Bosnia and Herzegovina. These have all been converted into the new monetary unit, the konvertibilna marka, and are fully backed by liquid the deutsche mark assets. The National Bank of Bosnia and Herzegovina and the NBRS have ceased to act as central banks.

Banks that used to do business in Bosnian dinars now transact in konvertibilna marka, and settlements among them occur daily in the books of the Central Bank of Bosnia and Herzegovina. This has required substantial coordination with the Payment Bureau in what was the Bosnian dinar area.

A main unit has also been opened in Pale, and the research department of the central bank—which is located there—is in the process of becoming operational.

What Remains to Be Done

Among the many tasks ahead to improve the operations of the Central Bank of Bosnia and Herzegovina, three stand out. The first is that the geographical area where konvertibilna marka transactions are routine must be enlarged. This requires passing appropriate legislation to allow such transactions, which are not permitted under the current payment system law, and establishing the main unit in Mostar. Both tasks have a political dimension that renders them complicated—but not impossible.

Second, while the konvertibilna marka exists for now only as a means of noncash payment—as electronic money—we need to introduce banknotes. These notes will be called kupons and will bear different entity design variants, one for each entity, although they will be legal tender throughout Bosnia and Herzegovina. The choice of the design has been a complicated political issue in the hands of the presidency of Bosnia and Herzegovina. Some progress is being made on this front and a resolution may be near.

Finally, the National Bank of Bosnia and Herzegovina will have to be liquidated. This will require bold action on the part of the Federation, as in the past the national bank has acted as a federation central bank—to a limited extent—a provider of credit to public institutions in part of the Federation. Similarly, the NBRS transformation into a different financial institution—mostly specializing in Yugoslav dinar transactions—will have to be completed.

Conclusions

The fact that the Central Bank of Bosnia and Herzegovina has been established successfully is a remarkable accomplishment. It has required the cooperation of all parties involved, and it shows that such cooperation is possible.

As the central bank expands its range of operations, the benefits of the new monetary regime will appear. It is expected that trade will be promoted both internationally and between the entities. This will be a key factor in promoting economic recovery and lasting peace.

Peace is a definite goal of Bosnia and Herzegovina, and with the support of the international community we are ready to build and keep peace on a long-term basis. At the same time, Bosnia and Herzegovina is fully aware that peacekeeping is directly dependent on its successful economic recovery and prosperity. The chances for economic recovery and for opening new roads leading to prosperity depend on:

- the efficient building—without delay—of an economic system based on transition to a market economy, a rapid process of privatization, and the creation of an atmosphere conducive to private investment;
- more efficient and rapid work by the institutions of both Bosnia and Herzegovina and the two entities as well as their mutual cooperation in the process of realizing a comprehensive economic program; and
- the scope and dynamics of international economic assistance and private investment.

The key problem in Bosnia and Herzegovina is employment, which can be solved only through economic reconstruction and economic growth. Therefore, the basic medium-term strategy in economics has to be based on stable macroeconomic policies, implementation and functioning of public and market institutions, structural reforms, and the reconstruction of housing and infrastructure.

Solid ground for such a strategy exists in using a fixed exchange rate and a currency board arrangement; exercising financial discipline, primarily in preventing the state, entities, and other levels of the authority from borrowing from the domestic sector; and continuing to receive international assistance on a broad basis and under good conditions.

The real increase in GDP for 1997 is estimated at 35 percent. Available domestic resources, supported by the international community and private foreign capital investment, especially to small and medium-sized enterprises, will have a dominant role in the realization of program goals. The Central Bank of Bosnia and Herzegovina will soon become fully operational, and we believe that it will be able to issue the new domestic currency. Further strengthening of financial institutions will continue, which will help to make a sustainable financial policy. Social protection for the most vulnerable categories and the creation of appropriate social programs are a high priority and will be a special concern of the entity governments.

In the beginning, macroeconomic structural reforms will be directed at customs tariffs and the further liberalization of trade, restructuring, and the privatization of enterprises and banks—on which certain legislature has already been adopted, while some of the laws—on education, health, pension system reform, and so on—have been submitted to the parliament for consideration and adoption.

During the coming months, we will continue our very successful cooperation with the IMF and World Bank staff, as well as with other institutions, aimed at working out and finalizing the comprehensive program of macroeconomics reforms that are necessary for the process of transition into a market economy.

We expect that we will soon be able to have an IMF arrangement, probably a Stand-By Arrangement, to support our economic program. The arrangement could be transformed into one under the Enhanced Structural Adjustment Facility in the first half of 1998 if the implementation of the Stand-By Arrangement goes well.

The needs for reconstruction, a social program, and the transition to market economy have to be consistent with monetary and foreign exchange policy (a currency board arrangement). All the budgets must be balanced, relying only on their own, regular revenues, without domestic borrowing. Fiscal policy should be a function of reconstruction and employment. Fiscal reform (fiscal federalism) and further strengthening of tax and customs administration are needed in the entities.

The budget of Bosnia and Herzegovina has been adopted in the amount of DM 136 million. The amount of DM 45 million will be allocated to meet the needs of administration, and DM 91 million is meant to service the external debt.

The entities are in charge of financing the administration proportionally, that is, two-thirds will be financed by the Federation, and one-third will be financed by the Republika Srpska. Furthermore, foreign debt servicing will be allocated to the entities, applying the criteria of the final user. An office in the relevant ministry is in charge of external debt management.

The essential problem of the state budget is that the state of Bosnia and Herzegovina is responsible for its international obligations, and the whole fiscal capacity, according to the current fiscal arrangement, is within the entities. We have been considering this problem, together with the international financial institutions and in line with the Dayton treaty, in an attempt to find a possible way of ensuring regular revenues for the budget of Bosnia and Herzegovina.

The fiscal system in the Federation of Bosnia and Herzegovina and the Republika Srpska is relatively well organized. The institutions of the fiscal sector have been established and function in an acceptable way; the elements of the dual system have been liquidated; and the revenues that belong to the different levels of authorities have been separated. Expenditures have also been separated, with a clear distinction as to what is financed out of each budget, regardless of whether that financing refers to administration expenditures, health financing, financing of education, or social programs.

In this context, special attention should be paid to controlling the entry and exit of goods at crossing borders, fighting against a “gray” economy and corruption, and putting all public financial courses under strict control.

Statement by the Governor of the Bank for Bosnia and Herzegovina

Hasan Muratovic

Please allow me to greet all of you, on behalf of the Council of Ministers of Bosnia and Herzegovina, and to thank you for all that you have done and are doing through the various forms of assistance that the international community, many of your governments, and many of you, personally, are providing to Bosnia and Herzegovina.

The government of Bosnia and Herzegovina closely follows the development of the new initiatives in the World Bank and the International Monetary Fund. We especially support the efforts of the President, Mr. Wolfensohn, to further the reforms under way in the World Bank. We are pleased with the first reports on the successful implementation of these reforms. We consider that, for borrowing member countries, it is of great importance to continue to work intensively on further decentralization of the World Bank. Decentralization improves the staff’s understanding of our problems and speeds up the implementation of projects. The exceptional performance of the Bank's Bosnia team in helping us with our problems is surely a model for other parts of the Bank.

Please allow me to inform you of several aspects of the ongoing and future reconstruction and development of Bosnia and Herzegovina, a country that suffered so much in the war. We cannot imagine the reconstruction of our country without international assistance and, in particular, the assistance of the Bretton Woods institutions, which provide such leadership to the rest of the world.

On the political front, it is my pleasure to inform you that just 10 days ago we had the first postwar local elections in Bosnia and Herzegovina, underlining clearly the democratic basis of our society.

Since the general elections, which were held last year, the most important task for us has been to create institutions at the state level and now, following the elections, at the local level as well. The establishment and work of the common institutions during this year has not been in line with the needs and expectations. However, with the assistance and friendly pressure of the international community, a number of institutions that are the foundations of Bosnia and Herzegovina have been established. The Parliament, Presidency, Council of Ministers, Joint Military Commission, Constitutional Court, and Central Bank of Bosnia and Herzegovina have been established. The parliament of Bosnia and Herzegovina has adopted a package of laws that are the framework of the economic system of the country: laws on the central bank, on customs policy, on customs tariffs, on foreign trade, and on external debt. A new domestic currency, the convertible mark (konvertibilna marka), has been introduced, and this currency is being used for noncash transactions in the payments system, covering some 80 percent of all monetary transfers.

In spite of political problems, we have also achieved a good start in the reconstruction of the country. As a result, the economic growth of Bosnia and Herzegovina in 1996, according to IMF and World Bank data, was as high as 50 percent, which is 15 percent more than expected.

We are pleased with the basic elements of the country assistance strategy recently adopted by the World Bank's Executive Directors, with increased International Development Association funds, which is the result of the successful implementation of previous projects. This strategy will allow the continuation of the technical-expert assistance of the World Bank in the consolidation and transition of the economy.

During this year, some of the first International Finance Corporation (IFC) projects are about to be realized in Bosnia and Herzegovina, and we have been preparing the first Multilateral Investment Guarantee Agency (MIGA) projects.

Finally, we have successfully concluded negotiations with the London Club on the rescheduling of our commercial debts.

All of these achievements have been made in close cooperation with the World Bank, the IMF, the European Union, and the Office of the High Representative, and with the enormous assistance of the U.S. Treasury. We would like to express our gratitude for their assistance. We owe our gratitude to the representatives of these organizations and bilateral donors in the field. I would like to use this opportunity to express our special gratitude to Mr. Wolfensohn for his personal commitment to and support for the reconstruction of Bosnia and Herzegovina.

There is no doubt that, of all donors, the World Bank has played the biggest role regarding the concept and implementation of the economic reconstruction, and for this impressive work we are profoundly grateful.

Unlike the Federation of Bosnia and Herzegovina, the Republika Srpska has received a smaller portion of assistance. The latest analysis shows that, at the beginning of this year, there was increased interest by donors in investing in Republika Srpska, so that the amount of assistance received could be multiplied in 1997. A number of projects—the realization of which is jeopardized by the present political crisis—are in the process of preparation.

Regardless of the good results achieved so far, the reconstruction needs of the country are still very high. At the moment, unemployment in the country is about 50 percent, while 60 percent of the population is dependent on humanitarian aid. For the housing sector, 85 percent of the accommodation capacity has to be reconstructed. Only 10 percent of the industrial capacity is utilized, and a number of companies cannot renew their production owing to a shortage of working capital. Two years after the cessation of war activities, Sarajevo still does not have its heating issue resolved, and water supply is restricted to only four hours a day. Regardless of the fact that repatriation is a priority, only 7 percent of refugees have managed to repatriate. Many things remain to be done, but the first priority is still housing and employment.

It is encouraging that in July 1997, albeit with a major delay, the Third Donors Conference for the Reconstruction of Bosnia and Herzegovina was held, the results of which are satisfactory. It is important for the donors and creditors to speed up the realization of their commitments. We believe that important progress in the implementation can be achieved by cofinancing the World Bank projects, using already established and extremely efficient organizations. As we are aware of the difficult economic situation in Republika Srpska, we understand donors' interest in economically supporting this part of Bosnia and Herzegovina to a larger extent than was the case last year. We support the attitude of the World Bank, despite the fact that it is not a political institution, in taking into account the level of cooperation of a certain area in the implementation of the Dayton Peace Agreement, while selecting the locations of realization of projects in Bosnia and Herzegovina. In that way, the World Bank escapes the danger of ruining the efforts of the rest of the international community in its implementation.

At all levels, Bosnia and Herzegovina's authorities have expressed their readiness for the future economic reforms. In both of the entities, the preparations for starting the process of privatization and banking system reform are under way. Although investment needs for physical and social infrastructure are still very high, we welcome the intention of the World Bank to increase, to a certain extent, its investments in projects aimed at providing support for economic reforms this year.

Unfortunately, although the majority of a future Stand-By Arrangement has been agreed upon with the IMF, the arrangement has not been signed yet. Commitments made during the conference last year have not been fulfilled. We have counted on the promised arrangement and on strong support from the International Finance Corporation. Because of the delay in connection with the Stand-By Arrangement with the IMF, we have not been able to begin our negotiations with the Paris Club and Bosnia and Herzegovina's arrears continue to accumulate. A number of other activities are affected by the arrangement with the IMF. We find the damage resulting from any further effects would be enormous, and much bigger than the expected benefits from these conditions; thus, we propose that the IMF arrangements for Bosnia and Herzegovina be realized without any further delays. We can assure you that we will work on the realization of the set conditions to the best of our ability.

We would urge the IMF to show more flexibility, so that we may have a Stand-By Arrangement and arrangement under the Enhanced Structural Adjustment Facility as soon as possible. Otherwise, all of the positive results that the international community has achieved for the economic reconstruction of Bosnia and Herzegovina could be jeopardized.

In the future, it will be necessary to have assistance in repaying Bosnia and Herzegovina's foreign debts. Regarding the total debt, of which a certain amount goes toward interest accumulated during the war, we have been considering the new possibilities for debt reduction with the World Bank. We need additional support in order to realize this aim.

We have been following closely the efforts of the World Bank and the IMF, aimed at securing a wide platform for fighting against corruption, which is a global problem, common to both developing and developed countries. We offer our strong support for these efforts. We find the guidelines for fighting against corruption recently adopted by the World Bank Board to be very useful. Last year, because we wished to ensure transparency in the realization of the foreign assistance, we established, in cooperation with the World Bank, the Agency for the Control of Supplies and Monitoring. For the time being, this agency is operational only in the territory of the Federation of Bosnia and Herzegovina, and we think that it is an imperative to establish this agency in Republika Srpska as well. We are proud that this agency, which consists of domestic and foreign consultants, has not found any cases of misuse during its work. In connection with this plan, we will continue our cooperation with the World Bank, to which we express our gratitude for its assistance in this field. Regarding the problem of corruption in the world, doubts and accusations having to do with corruption are very often the result of the political manipulations that almost always follow election campaigns. Political motives for accusations must be eliminated. Financial institutions and beneficiaries have to protect their reputations against frequent malicious accusations.

Allow me to propose that the World Bank and the IMF, together with the credit beneficiaries, create a fund for each project, on an obligatory basis, to monitor and control the implementation of the project. This will ensure that the credits will be used for their expressed purpose and that the reputation of creditors and beneficiaries will be protected.

Please allow me to express the desire of the Council of Ministers and all the citizens of Bosnia and Herzegovina to rely, as soon as possible, on their own resources in the country's economic development, and to lessen the extent of international assistance. We are fully aware that, in aiming for that goal, we have to bear the majority of the burden. As far as we are concerned, we are ready to realize the programs of economic reforms for which we still need significant international assistance and a substantial reduction of all debts.

Before I come to an end of my statement, allow me to express my congratulations to Cambodia and Turkmenistan for their membership in the IFC, and to Panama and the Dominican Republic for their membership in MIGA, and to wish them the most successful cooperation with these financial institutions.

Statement by the Governor of the Bank for Cambodia

Keat Chhon

As always it is a great honor and privilege to represent Cambodia at this august annual gathering of leaders and experts who shape and guide the world economy. I bring to you all greetings from the government and the people of Cambodia.

Our meeting here is of great significance to the world at large, as we are poised on the threshold of a new millennium that will dawn on us a mere three years from now. In the past 50 years since the coming into being of the two great multilateral financial institutions whose annual meetings we attend today, the world has witnessed many major changes and shifts. We have been able to adapt to these changes and challenges and devise instruments and mechanisms to steer effectively in the interest of stability and orderly growth. The challenges today are no less; indeed they seem to be new, more, and increasingly complex. We have witnessed just in the last three months how fragile and fickle the prolonged strong economic growth in this region has been. We have noted how much damage could be caused by speculative greed, shattering the dreams of the honest many, plunging governments and future generations into deep debt, and devastating the prospects for quick economic rebound and for employment opportunities. Eternal vigil is the price we have to pay in the future. And our two mighty financial institutions should set up warning signposts along the way through their annual reports and consultations with each country. We will no doubt discuss these matters here in this auditorium and in the lobbies around it. Cambodia, which is still an infant economy, will take lessons from here for adaptation at home.

In Cambodia, we are saddened by the events forced upon us in July 1997. As we have repeatedly explained, not taking any action at that time to nip in the bud the anarchic forces that were being let loose in our society, through clandestine dealings with outlawed genocidal elements by irresponsible politicians, would have meant plunging the country into a prolonged period of civil commotion and instability. Furthermore, it would have dealt a death blow to gains in democracy and freedom.

Since the removal of the anarchic elements, which by its nature was violent, and its immediate aftermath, Cambodia has sprung back quickly to normalcy. Rule of law, as well as law and order, has been fully restored, and security prevails in the country except in remote pockets on external borders where the rebels are active. In a transparent, clear, and fully free manner, new leadership has been elected and installed for the major coalition partner. The letter and spirit of our constitution, framed on the basis of the 1991 Paris Accords, have therefore been fully and openly observed and preserved. We have actively encouraged and assisted independent organizations to conduct full investigations into all complaints of human rights violations. We shall do all we can to bring culprits to justice. While no society can fully prevent crime, the test of its determination to protect people lies in its openness to criticism and complaints and the speed and energy with which it would address such complaints. We are doing just that. We are also determined to hold free and fair general elections and have already announced the date for the same, May 23, 1998. We are enacting necessary legislation to ensure a transparent process of elections under independent monitoring. International observers are most welcome to see for themselves all aspects of our electoral process. We have encouraged everyone, albeit a small minority, who left the country to come back to participate in the democratic process. We have repeatedly assured full protection to them within the legal framework. On the socioeconomic front, our new leadership has repeatedly assured that the progressive and proactive policies of the past would continue along with improving transparency and accountability of public governance.

We are somewhat surprised and saddened that, since these events and despite the decisive and quick action with which we have restored normalcy, freedom, and stability, some of our important external partners have either overtly, or without saying so, or in contrast with what they have said publicly, begun to slow down their support for the rehabilitation and development programs in the country, which are designed to serve the people at large. Development cooperation has to be a long-term commitment and should not be affected by misconceived perception of temporary events of a political nature, especially when the overall political framework, commitments, and promise for the future remain unchanged as in Cambodia today. Such setbacks to development cooperation undermines mutual confidence, affects the people at large, and retards progress, which alone is the bedrock for political pluralism and the many freedoms human beings cherish.

Let me now turn to the role of multilateral financial institutions in Cambodia. We are very grateful for the excellent assistance so far provided by both the IMF and the World Bank in financial, technical, and advisory terms. We look forward to continuing and strengthening the understanding that exists between the government and the two institutions. At the same time, I would like to emphasize that development is long term, and the delays and reductions in aid now imposed on us due to one-sided perceptions among some of our external partners would necessarily set the development clock back and make the development process that much more expensive and difficult to resume. Even when “domestic preoccupations” in some countries affect their will and ability to provide support to development elsewhere, it is vital and important that multilateral financial institutions like the IMF and the World Bank remain neutral and objective and act clearly professionally. They should desist from being drawn into a new post–cold war economic trap that some countries would like to set up based on misconceived political perceptions. These institutions should continue to provide support to Cambodia as before, even as they do in countries that are far less open and transparent even within our region. They should not slow down the process of their support. If they do, their proclaimed goals to reduce poverty would soon start sounding hollow.

I close with a plea that each country be allowed space and time to come up with solutions to its problems, be they political, social, or economic, as long as the chosen course is within the parameters of the basic principles of democracy, rule of law, and human rights that are universally agreed upon and are adhered to as in Cambodia. Let not the preconceived notions about the details of how a recipient country should govern itself be the guiding criteria for development support.

Statement by the Alternate Governor of the Bank for Canada

Huguette Labelle

Let me begin by expressing my appreciation to the government of the People's Republic of China for its impressive efforts in hosting this event and the warm hospitality that has been extended to all of us during these meetings.

The Canadian Picture

The macroeconomic policy framework that we have adopted in Canada—which focuses on putting the public finances on a sound basis and keeping inflation low—is now clearly paying off in the form of stronger growth and improved job creation. The Canadian economy expanded at a robust annual rate of 4.3 percent in the first half of 1997. This represents a significant strengthening in the pace of activity from the rate of 1.5 percent in 1996. Moreover, these recent numbers have prompted the IMF to raise its forecast of Canada's growth for 1997 as a whole to 3.7 percent.

Stronger growth is also translating into healthy job creation. The Canadian economy generated more than 260,000 jobs in the six months to the end of August, pushing the unemployment rate down to 9 percent. This performance suggests that Canada is poised to shortly attain the 300,000 jobs expected by private sector forecasters at the time of the February budget. Moreover, there is every indication that improved labor market conditions are helping to create a "virtuous circle" in which stronger employment growth leads to increased confidence that, in turn, results in continued overall growth.

The decline in interest rates and rise in confidence, which have contributed most directly to stronger growth, have been made possible by the remarkable progress that has been achieved by Canada's federal and provincial governments in reducing their deficits. Our financial requirements—a measure of the government's cash flow position—were in a surplus in fiscal 1996–97 for first time in over 15 years. On this basis, Canada's budgetary performance is the best among all the Group of Seven countries.

The World Economy

Turning to the international picture, the outlook for the world economy, on the whole, continues to be promising. Output, trade, and employment prospects have improved over the past year and further robust gains are expected next year. Moreover, the remarkable degree of policy convergence around the world—in particular, the strong commitment to low inflation and fiscal consolidation—suggests that current global expansion will likely be sustained. Nevertheless, risks remain. Our best protection against these risks, however, lies in the continued pursuit of sound domestic policies, international cooperation, and global integration as set out in last year's Declaration on Partnership for Sustainable Global Growth.

While the recent turmoil in Southeast Asian equity and exchange markets has highlighted the risks associated with global capital flows, we must not lose sight of the fact that these also convey critical benefits. An open and liberal system of capital movements improves the allocation of financial resources and can contribute significantly to global economic growth.

Institutional Achievements and Challenges

As we are all aware, the Fund has been actively promoting the orderly liberalization of capital flows for some time now. Broadening the IMF's authority to formally establish this activity as part of its mandate is long overdue. For this reason, I support an amendment to the Articles of Agreement, which would make the promotion of capital account liberalization a "specific purpose" of the IMF.

In the coming months, however, substantial work must still be done to determine the precise scope of the IMF's jurisdiction, as well as appropriate transitional provisions and approval policies. Close cooperation with other international institutions, such as the World Bank, the Organization for Economic Cooperation and Development (OECD), and the World Trade Organization, is essential to ensure that the IMF's jurisdiction is consistent with the work of these institutions. In our view, such cooperation would appear to exclude IMF involvement in inward direct investment, which is under discussion in these other institutions.

Turning to other IMF issues, I am pleased with the recent agreement on an IMF quota increase. I also welcome the agreement on a special one-time SDR allocation. This agreement will ensure that all members receive equitable treatment under all previous SDR allocations.

I would also underline the importance that we attach to recent progress to broaden the eligibility criteria and substantially increase the size of the Initiative for the Heavily Indebted Poor Countries. These changes will allow an even greater number of countries to benefit from this exceptional assistance. The next challenge is to ensure that this initiative is adequately funded. For our part, I am pleased to announce that Canada will convert its share of the second Special Contingency Account (SCA-2) refund into an unconditional grant of about SDR 12 million to support this initiative. For its part, the IMF needs an early discussion of the need to better "optimize" the use of its resources. It is also important that we encourage the Bank and the IMF to continue their efforts to press ahead in aggressively implementing this initiative.

I have also been impressed with Mr. Wolfensohn's efforts to bring about fundamental reforms in the World Bank through the "Strategic Compact." The progress report reviewing the concrete measures that have been undertaken in the first six months to improve the Bank's development effectiveness confirms that real change is taking place. Indeed, the Bank's commitment to reform is very much in keeping with the principles enunciated in the Development Assistance Committee strategy "Shaping the Twenty-First Century," which Canada has supported wholeheartedly. The Bank's efforts to more fully engage developing countries in partnership—to work more collaboratively with these countries as well as other donors—will be strengthened through initiatives, such as the decentralization of country programs, which are already under way.

Strengthening Good Governance

Let me also briefly comment on the recent work, which the Bank and the IMF have undertaken on governance issues. Last year, Mr. Camdessus and Mr. Wolfensohn emphasized that good governance is central to the basic economic objectives of both Bretton Woods institutions. This was recently underlined in the groundbreaking research in this year's *World Development Report* on "The State of a Changing World." The Bank and the IMF deserve to be commended for their efforts to move beyond rhetoric to provide practical guidance on these difficult issues.

The fight against corruption is of particular concern to the international community. As we are now acutely aware, corruption deters domestic and foreign investment and discourages private sector development. Moreover, the cost of corruption falls disproportionately on the poor, who are unable to pay bribes, and are therefore frequently denied essential services. In addition, widespread bribery undermines public trust in government and hinders the development of a well-functioning bureaucracy—both critical ingredients for economic and social development.

For these reasons, Canada is a strong supporter of action by the OECD to eliminate the favorable tax treatment that some industrial countries still provide for bribes. Canada also welcomes the promotion of a nonbribery pledge for all companies bidding on World Bank projects. In our own activities, we are pressing ahead to include anticorruption clauses in all contracts that are signed between Canadian companies and the Canadian International Development Agency (CIDA).

The Bank and the IMF can play a key role in addressing governance issues by bringing their unique expertise and experience to bear on the problem. I see the following opportunities for greater Bank and IMF involvement in the future.

First, both institutions can better integrate governance considerations into their operations. The IMF needs to do this in the context of its Article IV consultations and adjustment programs. The Bank needs to factor governance issues more explicitly into its policy dialogues, country assistance strategies, public expenditure reviews, lending programs, and project designs. In addition, both institutions need to take greater account of excessive military spending, especially when this comes at the cost of spending on basic health and education.

Second, the opportunities that exist for international cooperation on governance issues must be better exploited. Progress in areas such as money laundering and transnational bribery can only be made if all parties work together. In the future, this means greater consultation and sharing of information among the Bretton Woods institutions, regional development banks, the OECD and UN institutions, and bilateral donors.

Third, it is essential that a government have the capacity to provide a professional civil service, predictable and accountable policymaking, and a fair and transparent tax system. However, capacity building does not end here. Good governance requires the involvement of people in the decision-making process. For their part, the Bank and the IMF need to pay more attention to capacity building at the local level to help to better educate people to understand governance issues and provide viable forums for the exchange of ideas.

Finally, it is critical that information on best practices in such areas as efficient public sector management and effective tax systems be widely available. Developing countries that have the ability to retrieve such information have a marked advantage over those that do not. Indeed, the recent international conference, which Canada and the World Bank co-hosted on knowledge for development in the information age—Global Knowledge 1997—concluded that knowledge is increasingly becoming the basis for the wealth of nations, and for individuals to move out of poverty and take full part in economic, social, and cultural spheres.

However, knowledge, and the new technology that makes it potentially more accessible, will not automatically be accessible to all. Failure to consciously address issues of access to knowledge can aggravate existing problems of poverty and marginalization. For this reason, we wholeheartedly support President Wolfensohn's goal of making the World Bank into a "knowledge bank" and urge an explicit and concerted focus on the role of knowledge in poverty reduction.

Let me conclude by noting that the Bretton Woods institutions continue to face enormous challenges. However, we remain confident that they are fully capable of meeting these with flexibility and imagination.

Statement by the Governor of the Fund for Chile

Carlos A. Massad

I am honored to address this year's Annual Meetings on behalf of Argentina, Bolivia, Colombia, Costa Rica, the Dominican Republic, Ecuador, El Salvador, Guatemala, Guyana, Haiti, Honduras, Mexico, Nicaragua, Panama, Paraguay, Peru, Spain, Suriname, Trinidad and Tobago, Uruguay, Venezuela, and my own country, Chile.

The outlook for the growth of world output and trade for this year and the next is quite good. Even more important are the trends in factors contributing to the sustainability of global growth. Steady progress is being made in controlling inflation the world over, and the fiscal position of most countries is improving. Within this favorable global context, the Latin American economy is also making definite progress. Having overcome the weak performance of 1995, the region is set to grow by more than 4 percent in 1997, a higher rate than the 3.4 percent recorded in 1996. Particularly noteworthy is the significant recovery of the Argentine and Mexican economies. We can also expect faster regional growth by 1998.

Together with this improved outlook for growth in the region, capital inflows—that already in 1996 were at high levels—have continued to increase, a clear reversal of the temporary scarcity Latin America faced in 1995. Indeed, the Economic Commission for Latin America and the Caribbean estimates that capital inflows in 1997 will amount to approximately $70 billion, some $15 billion more than the projected current account deficit. Progress with regard to inflation recorded over the last three years is continuing. The regional inflation rate for 1997 is expected to be one of the lowest this century.

However, much remains to be done. To accomplish these tasks, rates of domestic saving and investment in physical capital must be raised, and education and health services must be radically improved. In that regard, perhaps what is most needed is to avoid the cycles of excessive growth followed by recessive adjustment that have been the hallmark of the region for almost two decades. To this end, inflation control should be a priority, and timely preventive action should be taken when signs of deterioration in inflation rates or the external position appear. Both conditions, namely domestic and external equilibria, can be met through a sound fiscal position, which ideally should also be flexible, so as to support monetary policy in achieving stabilization. Domestic macroeconomic policies must also be compatible with the exchange regimes adopted. Progress in this area is promising.

However, good fiscal management alone is not enough and is often hard to reconcile with far-reaching policies for improving equity and competitiveness, unless the proper instruments are in place for coping with private sector expenditure cycles. Development of a sound framework of prudential regulations and financial supervision, which our countries are working toward, is essential for ensuring the proper channeling of domestic and external financial saving into profitable ventures with a high probability of repayment. Too much private spending, financed by a poorly regulated and supervised financial system, may have been a determining factor in the recent financial and balance of payments crises in the emerging economies.

Equally as important as proper domestic policy management is a stable international environment. In that connection, although projections of world growth for this year and the next are positive, we should not underestimate a number of risks that are looming on the horizon.

The last two years have been characterized by ample international liquidity and the continued strengthening of the U.S. dollar. This abundance of liquidity has greatly benefited many economies. However, the pressure of this liquidity on the level of domestic spending in recipient emerging economies has been a factor in the significant widening of balance of payments current account deficits. In some cases, these deficits have increased beyond sustainable levels. This has triggered crises in a number of places and the contagion has spread worldwide. Experience has shown that policy changes in the developed countries can have a major impact on the developing countries. Developed countries, and also the Fund, must be mindful of the systemic effects that may arise from such changes.

In this context, continued stable conditions on international financial and exchange markets are of paramount importance, given countries' increasing openness to international capital movements—one of the key issues addressed at these meetings. Although progress on inflation and fiscal consolidation suggests that the moderate real interest rates on international markets of late should not significantly change in future, there are nevertheless some disturbing signs.

The U.S. economy seems to be operating at a sound and sustainable pace. Despite the absence of inflationary pressures in the goods and services markets, the sharp rise in asset prices, a phenomenon that has not yet been fully analyzed and has spread to many emerging economies, is a cause for concern. As for continental Europe, the advent of Economic and Monetary Union (EMU) will have major, and potentially positive, global repercussions. We are confident that the commitment of the European Central Bank to combating inflation will counteract any possible risks. In the case of Japan, the second quarter of this year was marked by sluggish performance and this is not an encouraging sign. There is considerable need for more vigorous growth both in Japan and in the economies that export to Japan, especially those in Asia that have recently been suffering financial and exchange problems.

The points I have raised demonstrate the high level of interdependence in the world economy today and the growing importance of balanced development. Let me offer some thoughts on the proposed amendment of the Articles of Agreement of the International Monetary Fund, with regard to the broadening of its jurisdiction over international capital movements.

The representatives of the countries in the region have clearly expressed their willingness to extend the Fund's mandate to enable it to promote liberalization in the capital accounts of its member countries. The requirement that external saving should supplement domestic efforts to tap our vast investment opportunities will create an environment in which we can obtain additional sources of financing, with better maturities and prices. No less important is the opportunity to diversify our own financial assets to incorporate instruments from a wide variety of countries, so that the profitability and risks for large amounts of personal savings, such as those invested in pension funds, will no longer be so dependent on domestic economic cycles.

By broadening the Fund's jurisdiction, it will be possible to ensure that the natural process of deregulation that is spontaneously occurring will be more orderly, efficient, and balanced. To maximize this potential, however, it is necessary to ensure that the new wording of the Articles provides the flexibility and powers needed to properly guide the process.

The Fund's Executive Board discussed using a transition period to enable the countries regulating capital flows to phase out these restrictions. This period, its definitions and approval policies are of main importance. Precipitate liberalization would create new financial crises with a spillover to other countries resulting from the contagion effect.

A transition period is not sufficient. In our opinion, one of the most important aspects of the future regime is the treatment of prudential measures. Owing to the structural characteristics of the economies of our region—mostly small open economies requiring external resources and with insufficiently diversified exports—they are highly vulnerable to external shocks. Although this vulnerability can be lessened with proper macroeconomic management, the volatility of some key variables cannot be completely prevented. This volatility has a very considerable effect on the stability of the financial system. Thus, adoption of prudential regulations in the financial system is very important to prevent any macroeconomic disturbance from being amplified into a full-blown crisis.

It has been proposed that the guiding principle for prudential regulations should be to exclude any relating to balance of payments or macroeconomic management reasons. However, prudential regulations applicable to the financial system are specifically designed to prevent financial problems that are initially limited or microeconomic in scope from acquiring macroeconomic proportions. Thus, the decision to exclude a regulation based on its macroeconomic character could be arbitrary and even inappropriate. Take, for example, the case of a rapidly growing economy with sound fundamental balances. The high rate of return on capital in a booming economy attracts large inflows of external resources. These inflows are further encouraged by the appreciation of the domestic currency, which is characteristic of economies experiencing rapid productivity growth. Capital inflows stimulate domestic demand and could push up domestic interest rates if the monetary authorities safeguard domestic equilibrium. This, in turn, could provide a further incentive for capital inflows. The probable outcome will be continued appreciation of the real value of the local currency, the resulting risk of widening the current account deficit, and the greater danger that these capital flows will be reversed, should some negative external shock occur. After implementing all the so-called first-best solutions, such as fiscal consolidation, incentives for capital outflows, and strengthening of bank supervision, the authorities may in addition have to take measures to discourage short-term foreign borrowing in order to minimize the impact, particularly on the financial system, of a possible reversal of capital flows. Would not such measures be eminently prudential? Could not the same be said of a requirement that high levels of liquidity be maintained in the financial system of an economy that is sound but risks contagion from an unstable neighboring economy?

In our opinion, the appropriate criteria for admitting prudential regulations should be based on a review of the status of economic fundamentals and not on the assumed micro- or macroeconomic character of the regulations. If the fundamentals are in order, prudential regulations will in fact be preventive or prudential in nature. If, on the contrary, this is not the case and adjustments need to be made, countries must take action to correct these fundamental imbalances before resorting to regulations or restrictions that, quite probably, would be used as substitutes for the necessary adjustments or would have a very limited effect if markets were aware of the fundamental imbalances. Prudential regulations are complements to, not substitutes for, the maintenance of sound fundamental balances.

In this new age of increasingly fluid capital markets, the role of international financial institutions is also affected. For the Fund, balance of payments crises will continue to emerge. Though such crises will probably be less frequent, they may well be more severe; thus, continually reviewing the modalities of the different available lending facilities will be an important future task of the Fund. We must also endeavor to provide the Fund with adequate resources and further facilitate drawings by member countries as the volume and scope of private capital movements increase.

In that connection, we welcome the agreement reached on the allocation of special drawing rights, an issue that was subject to lengthy discussions. The Fund's Executive Board has also reached a consensus, to be ratified by the Board of Governors, on the Eleventh General Review of Quotas, requesting an overall increase of 45 percent. This consensus was not easy to attain, mainly because of the difficulties in reaching an agreement on criteria to distribute shares on a proper method for power sharing among members. An in-depth and informed discussion on the calculation of quotas would be very desirable. In any event, we regret that, under the current review, the developing countries, which have for some time now been recording substantially higher growth rates than the other countries, stand to lose some of their relative weight. We hope that, as a result of reviewing the formulas, this situation will be corrected in future. Meanwhile, we trust that the commitment to maintain the current representation will be honored.

Allow me to refer to my own country for a moment. The performance of the Chilean economy in recent years has meant that, in macroeconomic terms, the 1990s will undoubtedly be the best decade of the twentieth century. During this decade, Chile has achieved a high and sustained economic growth rate averaging more than 7 percent a year, while steadily reducing inflation gradually from almost 30 percent a year in 1990 to an estimated 5.5 percent in 1997. The current account deficit has been maintained at perfectly sustainable levels, averaging less than 2 percent of GDP for the decade to date and peaking at just about 4 percent of GDP. At the same time, exports have continued to grow at a sustained rate that exceeds the GDP growth rate.

In the area of social development, during the past 10 years, the incidence of poverty has been virtually cut in half, thereby reducing the percentage of persons with incomes below the poverty line from almost 40 percent of the total population in 1987 to just over 20 percent in 1996. The results were even more favorable in the case of extreme poverty, which in 1996 was reduced to one-third of the level of the mid-1980s.

We consider these favorable results to be the product of serious efforts reflecting the commitment by the Chilean authorities to maintain macroeconomic equilibrium and achieve sustainable performance in the medium term. This commitment is reflected not only in the policies followed by the government, but also by the central bank, whose autonomy and independence were established by law more than seven years ago.

The macroeconomic program for 1998 plans to maintain rapid economic growth, at a rate of 6.5 to 7 percent a year, and to continue to gradually reduce the inflation rate, aiming at a level close to 4.5 percent—1 percentage point less than the target for this year. The fact that inflation targets for each of the past few years have been achieved and that the policies followed have been consistent has given credibility to the stabilization effort. Owing to careful regulation of capital flows, particularly the prevention of rapid increases in foreign borrowing, significant and sustainable advances have been made in Chile's integration into the external financial arena. As a result, the cost of foreign borrowing has significantly decreased and the composition of external financing has improved, with emphasis on foreign direct investment and long-term borrowing.

The success of these tasks is not only the result of the determination of the monetary and financial authorities; another key element is fiscal consolidation, which has resulted in repeated government finance surpluses, high levels of public saving, and moderate expenditure growth. This path of careful moderation must be pursued if success is to be achieved.

Policies to maintain macroeconomic stability will enhance the sustainability of the improvements in growth and development. This development will enable one-fifth of all Chileans, who still live in conditions of poverty, to enjoy the increasingly abundant fruits of progress. Sharing the fruits of progress is ultimately the foundation of social cohesion, institutional development, and democracy.

Statement by the Governor of the Bank for the People's Republic of China

Liu Zhongli

The world economy continued to be encouraging in 1996 and achieved its best performance since 1990. The integration of developing countries in the world economy was further strengthened. However, we should not overlook the wide range of risks and fragilities persisting in the world economy. The international financial market has experienced some unrest. International capital flows have created opportunities for developing countries, as well as risks, such as speculative attacks. Global inflation could rise, causing interest rates in developed countries to increase, thus reducing capital flows to developing countries. Especially disturbing is that official development assistance (ODA), as a share of developed countries' GNP, has dropped to the lowest level in 50 years. New protectionism is occurring in international trade under the guise of environmental protection and labor standards. These problems, if not addressed in a timely and effective manner, will not only dampen the economic future of developing countries, but will also undermine the sustainability of global economic growth. We call upon the international community, and developed countries in particular, to act as soon as possible to reduce uncertainty and destabilizing factors in the world economy.

China's economy has made satisfactory headway in 1996, and, since the beginning of 1997, the economy overall has maintained a momentum of healthy growth. While encouraged by our prospects, we are fully aware of the challenges we face. China is still a low-income developing country with a large population, a weak economic base, and wide disparities across regions. At present, we are facing a number of difficulties, especially irrationality in the economic structure, low efficiency in the economy, heavy losses by some state-owned enterprises, and rising unemployment. To address these problems, the Chinese government will further enhance economic system reform and take effective measures to change the growth pattern. Particularly, we will speed up the reform of state-owned enterprises, focusing on invigorating the larger ones while further relaxing control over the smaller ones. We will standardize bankruptcy procedures, encourage mergers and acquisitions, and promote reemployment. We are fully confident that, within the next few years, the performance of state-owned enterprises will be improved fundamentally. At the same time, we will continue to readjust and improve the ownership structure, and efforts will be made to develop diverse forms of ownership while ensuring a dominant position for public ownership.

The World Bank, as the largest international financial institution, has played an important role in supporting economic development in developing countries. We note that the Bank's management, and Mr. Wolfensohn in particular, has exerted much effort in promoting the Bank's own reform. We support the fundamental objectives of the Strategic Compact, namely, to increase the efficiency of the Bank's work and provide better and more timely services to its borrowing members. In designing and implementing reform measures, the Bank should fully consider the real needs of different borrowers. In today's changing world, it is important, more than ever, that the Bank act strictly within its mandate and overcome any political interference. We hope that the Bank will make full use of its comparative advantages and continue to focus on transferring resources to developing countries, alleviating poverty, and promoting sustainable development as its core operations.

International experience has shown that infrastructure development requires joint efforts by the public and private sectors. In this vein, we support the World Bank Group's role in taking action, including strengthening and expanding guarantees, advisory services, and information dissemination, in order to facilitate private sector involvement in infrastructure. At the same time, we are of the view that the ability to provide finance is a valuable asset of the Bank and that financing infrastructure in developing countries directly should continue to be a priority for the World Bank and other multilateral development banks. In the future, the Bank's role in infrastructure, particularly in those projects related to poverty reduction, will still be irreplaceable. The Bank's finance in infrastructure will not crowd out the private sector; on the contrary, it will help create an enabling environment for private sector participation.

We note that the prospects for the Bank's net income are less than optimistic. We are of the view that the Bank must be more selective, especially when it is faced with increasing claims. In allocating net income, priority should be given to supporting the mainstream operations of the Bank as a development institution, especially lending, and the principle of equity should be observed.

The Multilateral Investment Guarantee Agency (MIGA), since its founding, has played a unique role in helping developing countries absorb international capital. We welcome the consensus reached on MIGA's capital increase and are willing to take our share of responsibility.

Improving governance and eliminating corruption contribute to economic development. Fundamentally speaking, the responsibility for fighting corruption rests solely with sovereign governments. The Bank and the IMF, at the request of countries concerned, could play a useful role. But the two institutions should act in strict accordance with their respective mandates, limit their anticorruption activities to the economic aspects, and ensure uniformity of treatment of all members based on objective criteria.

We are pleased to see that certain progress has been made in implementing the Initiative for Heavily Indebted Poor Countries. We hope that creditors, especially the Paris Club members, will honor their commitments in a timely manner to benefit eligible countries as soon as possible. With regard to the debts owed to China, we will address them through bilateral channels on a case-by-case basis.

The Chinese government supports the IMF's efforts to assist the economic reforms and adjustments of developing countries through arrangements under Enhanced Structural Adjustment Facility (ESAF). It is our view that the major industrial countries should take the lead in making concrete financial commitments. Conditional on this, China is willing to consider contributions comparable to its fiscal ability.

We support the extension of the Fund's jurisdiction to the capital account, and we endorse the inclusion of capital account convertibility in the Fund's purposes. Meanwhile, the Fund should respect the sovereignty of member countries and the jurisdiction of existing international treaties. Sufficient time should be given to member countries to study related issues, and haste should be avoided. During the transitional period, those members with immature conditions should be allowed to proceed in an orderly and healthy manner based on their real situations. Technical assistance to member countries should also be strengthened.

We welcome the newly reached agreements on the SDR allocation and the quota increase under the Eleventh General Review. Developing countries' quota share in the Fund and capital share in the World Bank are declining, however. We ask that efforts be made to address this issue at an early date.

As is well known, the return of Hong Kong to China has increased China's economic strength. This development should be duly reflected in China's quota share in the Fund. China has made a formal request to the Fund for a special increase in its quota share. We hope that our reasonable request will be met as soon as possible.

Statement by the Governor of the Bank and Temporary Alternate Governor of the Fund for Colombia

José Antonio Ocampo Gaviria

It is a great honor for me to address these Annual Meetings of the World Bank and the International Monetary Fund on behalf of Latin America and of my own country, Colombia.

Let me start by expressing our gratitude to the government of the People's Republic of China and to the authorities of the Special Administrative Region of Hong Kong for their hospitality and outstanding organization of this forum.

Latin American Growth and Capital Volatility

The year since the previous Annual Meetings has been a period of acceleration of economic growth in our region. The strong recoveries in Mexico and Argentina, after their 1995 recession, have been accompanied by more rapid economic growth in Brazil. More recently, among medium-size economies, Peru and Colombia have shown clear signs of acceleration after their 1996 slowdown, as Venezuela recovered from her recession. Chile has continued, in turn, on her solid expansion path. Projected growth rates for Latin America, of 4 percent or more for 1997, reflect a generalized improvement of economic performance in the region.

Medium-term prospects have also improved. The new *Global Economic Prospects* projection for the region for 1997–2006, 4.2 percent a year, is a clear demonstration of this fact. However, this rate of growth remains below that which the region achieved prior to the 1980s, and that which is necessary to overcome the pressing economic and social problems we face. The region must thus continue to build, through structural reforms, the conditions to accelerate economic growth.

An essential element of this process was the rapid normalization of capital flows after the Mexican peso crisis in late 1994. The renewal of private capital flows has been accompanied by improved spreads and country rating upgrades. It is important to emphasize that the recovery in the region in the aftermath of the Mexican crisis, as opposed to the devastating effects of the debt crisis of the 1980s, was largely determined by the rapid intervention of multilateral agencies. This stresses the crucial role these agencies play in avoiding sharp fluctuations in capital flows. We thus welcome the timely response of the Fund to the recent problems faced by some Southeast Asian countries.

Capital volatility will continue to be a major source of instability for the region and for the developing world as a whole. It is true that domestic policy weaknesses have sometimes contributed to such instability. This is not the full story, however. It is clear that the Mexican peso crisis in 1994 was worsened by the panic behavior of short-term capital flows, which blew the crisis out of proportion with regard to its initial fundamental factors. Speculative behavior has played again a destabilizing effect in the recent Southeast Asian events. In both cases, contagion effects spread the crisis to other countries, including those with sound macroeconomic management.

This is the background against which the issue of capital market liberalization should be analyzed. For several Latin American countries, price-based capital controls have proven to be an efficient mechanism to discourage short-term capital flows and to reduce the volatility of domestic credit and exchange rates. They provide, in turn, incentives for long-term capital inflows and restore some degree of autonomy that policymakers may have lost in the process of economic and financial liberalization. This is why we fully support the Group of Twenty-Four (G-24) declarations, which emphasized that “precautionary and price-based measures could help countries protect economic stability and sound macroeconomic management.”

Moreover, financial liberalization must be accompanied by stronger multilateral institutions, capable of effectively compensating the instability of private capital flows. In this regard, as well as that of the Multilateral Investment Guarantee Agency (MIGA) and the Initiative for Heavily Indebted Poor Countries (HIPC Initiative), there has been a wide gap between the increased responsibilities given to multilateral agencies and the willingness of some shareholders to effectively provide them with an adequate capital or quota base.

World Bank Initiative

Let me use this opportunity to congratulate the World Bank for its 1997 *World Development Report,* as well as for its recent reform agenda for Latin America, which was issued under a very Chinese title, *The Long March*. They deal, no doubt, with very controversial subjects but will, nonetheless, become crucial references for the ongoing debates on the redesign of the state.

The reform process under way in the Bank is, no doubt, essential to guarantee a more effective client-oriented institution, though its risks should not be disregarded. Loans denominated in single currencies, adjustable loans, portfolio management, decentralization, and support to private infrastructure are moves in the right direction. Much more remains to be done, however. To mention just two crucial issues: project approval continues to be cumbersome, and national government guarantees are increasingly paradoxical for an institution that wants to give direct support to local governments and to the private sector.

Let me focus my attention on three issues that are central to the discussions going on at these Annual Meetings: World Bank involvement in efforts to combat corruption, the HIPC Initiative, and support to private sector infrastructure.

We fully support international efforts to combat transnational bribery, asset laundering, and other forms of economic crime. My own country, Colombia, has been deeply involved in encouraging international treaties and domestic legislation to combat corruption and asset laundering, and thus strongly supports World Bank involvement in the fight against corruption and its transnational dimensions. At a national level, such involvement must obviously be based on objective analysis and established facts, and it should be concerned with systematic corruption rather than with isolated cases.

We are deeply concerned about the slow progress in the implementation of the HIPC Initiative, which basically reflects the financial uncertainties it faces. Let me also express this point of view in the name of the Non-Aligned Movement, which Colombia currently chairs. It is urgent that full funding be guaranteed to the HIPC Initiative as well as to the Enhanced Structural Adjustment Facility. This includes the adequate funding for regional multilateral institutions by their members, and, in the particular case of the African Development Bank, by special contributions from industrial nations. Moreover, this process should not weaken the financial strength of multilateral institutions. In this regard, we view with increasing concern the additional use of IBRD's net income for this purpose, and prefer mechanisms in which the required resources are explicitly provided by its members. We are willing to share in such costs, as well as in those of other multilateral institutions to which we belong, following equitable sharing and transparent rules.

We strongly support the action program on private infrastructure presented to the Development Committee. Obviously, involvement in this area should complement and not substitute traditional support to public sector investment in infrastructure, which will continue to be essential. Collaboration between Colombia and the Bank in private infrastructure has been very productive, as the action program recognizes. Based on that dialogue, let me refer to six areas that are essential to the success of this initiative.

The first area is the close collaboration among the World Bank, the International Finance Corporation, and MIGA in this area. The design of country assistance strategies must emphasize this coordination among Bank Group institutions. Second, although adequate project design should minimize—or even eliminate altogether, in some cases—the use of government guarantees, contingencies assumed by governments should be adequately estimated and budgeted. Third, the adequate weight of guarantees versus loans in the determination of overall World Bank financial support to a specific country must be urgently analyzed, for otherwise guarantees will become an unattractive alternative. Fourth, guarantees should not necessarily be the major source of IBRD financial support. The Bank should also support the design of infrastructure financial facilities that guarantee the rollover of project financing when it matures, and of national and regional infrastructure funds, particularly those that participate in the financing of medium-size projects. Fifth, this should be complemented by programs to develop local capital markets, which should provide an increasing proportion of financing in this area. Finally, private financing of infrastructure is a clear case in which the Bank should consider the elimination of government counter guarantees as a condition for Bank financing.

The Colombian Economy

Let me finish with a brief statement on the Colombian economy. GDP growth slowed down in 1996 to 2.1 percent. Although several factors contributed to this process, a major reason was the contractionary monetary policy implemented by the central bank to face a clear overheating of the economy at the end of the 1992–94 boom, during which aggregate domestic demand increased at unsustainable levels: an average of 11 percent a year, compared with a GDP growth rate of 5 percent.

Since the second quarter of this year, economic conditions have significantly improved. GDP, seasonally adjusted, grew 3.7 percent during the quarter. Preliminary third-quarter data indicate that this trend has continued. We can expect rates of growth of more than 3 percent for 1997 as a whole and close to 5 percent for 1998. Inflation has come down simultaneously, though much more should be done in this area over the next few years. Annual inflation came down from 21.6 percent in December 1996, to 18.0 percent in August—this year's central bank target. The trade and current account deficits are simultaneously decreasing, and we have been able to correct part of the undesired real appreciation that we faced during the second semester of 1996. This has been consistent, moreover, with unprecedented levels of foreign direct investment, which could reach $5 billion this year—equivalent to 5 percent of Colombia's GDP.

Finally, economic recovery and the austerity measures adopted for 1997 have been reflected in stronger fiscal accounts than originally projected. This process will continue in 1998, as the austere budget before Congress indicates. Central government expenditure, net of interest payments, will fall by more than 1 percentage point of GDP between 1996 and 1998. Tax revenues have simultaneously increased 14 percent in real terms over the past four months. This will allow a reduction of the operational deficit of the consolidated public sector to 1.5 percent of GDP this year, and to return to an equilibrium operational position in 1998. This shows our strong commitment to sustainable recovery and to traditional orthodox standing in fiscal policy.

Statement by the Governor of the Bank for Cyprus

Christodoulos Christodoulou

It is a great pleasure and honor for me to address these Fifty-Second Annual Meetings of the International Monetary Fund and World Bank.

It is encouraging that the world economy over the past year has been characterized by healthy growth, low inflation, reduced fiscal deficits and significant structural reforms in a number of countries. This improvement in the economic fundamentals has enabled many countries to pursue new initiatives and reforms to meet the challenges of globalization. At a regional level we welcome particularly the historically high economic growth rates being recorded by sub-Saharan Africa and the resumption of positive economic growth in the countries in transition and trust that these developments can be sustained.

The benefits and costs associated with the globalization process for emerging market economies has been illustrated strikingly during 1996 and 1997. Massive amounts of foreign private capital have flowed into these economies, especially to Southeast Asia, to promote investment and rapid economic growth. However, the vulnerability of such flows to individual countries and regions in response to shifts in market sentiment has been underlined by the recent downward pressures on the currencies of a number of Southeast Asian countries and the large falls in equity prices in their markets. We need to put these developments into perspective and assess whether foreign investors and financiers and domestic players have exaggerated the deterioration in the prospects for Southeast Asian economies and have overreacted by shifting funds and capital out of these countries. If so, what else can the international financial community, including the IMF, do to help restore confidence in the currencies and financial assets in the affected Asian markets? Are the IMF's resources too limited to provide quickly the appropriate amount of emergency financing? What corrective measures should the authorities of individual countries take to enhance and reinforce policy credibility in the eyes of domestic and foreign investors? It is pleasing to note that the Interim and Development Committees have in recent days been at the forefront in addressing these issues.

In Cyprus we have become acutely aware of how sudden shifts in investor and consumer confidence arising from actual and perceived political and military developments can be transformed quickly into destabilizing financial and economic developments. In 1996 events, which caused uncertainty regarding future political and military developments, depressed foreign and domestic spending in the Cyprus economy reducing the growth rate to 2 percent compared with 5½ percent in the preceding year. To contain the destabilizing tendencies the economic authorities stressed the good economic fundamentals pertaining to the Cyprus economy and its ability to increasingly align its policies with those of the more successful performers in the European Union. Indeed in 1996, with a stable exchange rate, annual inflation about 2.1 percent according to the interim EU harmonized consumer price index, a long-term interest rate of 7 percent, and a public debt to GDP ratio of 54 percent, Cyprus was able to meet almost all of the Maastricht criteria. Only a government deficit to GDP ratio of 3.4 percent, caused mainly by a moderation in the growth of revenues, prevented full satisfaction of the Maastricht criteria. In 1997 a strong recovery in net exports is now boosting the growth performance of the economy, while the rates of unemployment and inflation have been about 3 percent.

We consider the issues of the ability of the IMF and World Bank to help promote and sustain economic growth in the least developed countries and to provide emergency financing to countries affected by sudden private capital outflows are of great importance. The IMF and the World Bank must have the financial resources to respond quickly, flexibly, and adequately to meeting such responsibilities. We welcome the approval of the increase in quotas by 45 percent, a measure that will enhance the ability of the Fund to deal more adequately with balance of payments and currency crises of its members. Cyprus welcomes also the recent decision of the IMF to proceed with a new SDR allocation.

Cyprus would support efforts being made to speed up the implementation of debt initiatives by the IMF and the World Bank to assist the poorest highly indebted countries. We are concerned also that the flow of official and World Bank development assistance to African countries is falling and would urge that greater efforts be made to address this problem.

In concluding, I would like to stress that Cyprus will continue to support and cooperate with the Fund and the Bank in their efforts to foster a stable economic environment conducive to growth and development. I would like also to take this opportunity to thank the management and staff of the Fund and the Bank for the constructive advice and assistance they have rendered to Cyprus. In particular, the various missions that have visited Cyprus in recent years have been instrumental in enabling us to implement economic and financial reforms that were necessary to liberalize our economy and to harmonize our policies and institutions with those of the European Union.

Statement by the Governor of the Bank for the Arab Republic of Egypt

Atef Mohamed Mohamed Ebeid

I am pleased and honored to address this gathering on behalf of the Governors of the Arab member states of the World Bank and IMF. I would like to begin my remarks by congratulating you on your election to chair the Board of Governors this year, and by thanking the government and citizens of the People's Republic of China for their kind hospitality and successful organization of this year's meetings.

During the past year we have witnessed a number of important developments in the global economic environment, including the continued pursuit, in a large number of countries, of policies aimed at achieving fiscal and monetary stability. These policies have led to reduced budget deficits and lower rates of inflation and world interest rates, and have helped to create a favorable economic climate in most countries of the world. Many countries have continued their structural reform efforts, which have helped to improve prospects for continued economic growth. But these developments were not accompanied by increased growth rates or by a reduction in the high rates of unemployment prevalent in many European industrial countries, although there are encouraging signs of increased economic activity in a number of them. While the lower economic growth and higher unemployment in these countries reflect in part a reduction in their budget deficits, we believe that additional efforts must be made to eliminate labor market distortions and reduce unemployment by increasing the flexibility of wages and improving the social safety net.

On the other hand, economic growth in 1997 remained strong and without inflationary pressures in the United States and the United Kingdom, two countries distinguished by their flexible labor markets and balanced economic policies.

A number of countries in transition have implemented economic reform policies over the past few years that have significantly increased economic activity after a period of stagnation. In the developing countries, where reform efforts have been redoubled, growth rates remain high. We are highly appreciative of the efforts being made in developing countries, and of the outstanding role played by the World Bank and the IMF in supporting the implementation of sound economic policies in their member states.

On this occasion, and in order to support efforts to promote growth in developing countries, we call on the industrial countries to eliminate the obstacles that still constrain the exports of developing countries. We also hope that the reserve currency countries will intensify their efforts to reduce fluctuations in the exchange rates of their currencies, as such fluctuations have a negative effect on the economies of developing countries, especially those tied to the exchange rates of the principal currencies.

The global economy is currently undergoing great changes. The globalization of financial markets and the elimination of constraints to international trade have led to a new challenge—not only for the Bretton Woods institutions, but also for the policymakers of their member countries. Although the new economic environment has led to the creation of investment opportunities and worldwide growth, it has also resulted in new challenges for the member countries and the international financial organizations, including the increased size and sophistication of world financial markets, advances in information technology, and increases in the size of capital flows and the ease of transfers between various financial markets. The Bretton Woods institutions have a particularly important role to play in helping their member countries, especially the developing countries, to take full advantage of this new climate, while reducing the associated risks. Recent developments have caused the IMF to consider amending its Articles of Agreement to allow it to supervise efforts aimed at liberalizing worldwide capital movement, to ensure that it is done in an organized and effective manner. The recent problems of financial markets in many emerging markets are largely the result of the increased globalization of these markets. In order to obtain the maximum benefit from globalization and to minimize its negative effects, many developing countries have implemented a series of sound economic reforms, accompanied by comprehensive structural reforms. But these measures alone are not sufficient, as recent developments in Southeast Asia have shown. Even countries that follow sound economic policies are not safe from the effects of financial disturbances in the region.

Recent global developments have underscored the need, when preparing economic reform programs, to consider the existence of favorable conditions in the countries concerned, which will allow them to meet the challenges of integration into the global financial markets.

It is also crucial to ensure that the financial and banking sectors are sound, and to strengthen financial markets in the developing countries, thus enabling them to keep pace with the latest economic developments. Here I would like to stress the importance of the technical assistance provided to developing countries by the IMF and the World Bank, to support their efforts aimed at integrating themselves into the new world order. There is no doubt that globalization has added to the burden of responsibilities carried by the World Bank and the IMF, and we consider the rapid response of the two organizations to the crisis in Southeast Asia to be clear proof of their effective role in limiting the effects of financial crises.

We endorse the importance attached by the Bank and the Fund to the role of sound management in economic development, but the focus must be on strengthening the economic aspects of sound management, as these lie naturally within their scope of activity. We also stress the importance of respecting the sovereignty of the member states and their freedom to choose the type and timing of the programs they implement. We also welcome the increased importance attached by the Bank and the IMF to the social dimension of economic reform programs in developing countries, especially in two areas: first, providing the needed resources to the health and education sectors within the framework of economic reform programs, as it is very difficult to achieve sustained high rates of growth without developing human resources; second, establishing effective mechanisms to provide a social safety net as an integral part of reform programs, as such mechanisms to reduce the negative effects on limited-income groups during the early stages of reform, while helping to promote public acceptance of the reform process itself.

We support the international initiative aimed at reducing the burden of heavily indebted poor countries, but we would like to express our concern over the unavailability of sufficient resources for this purpose. If sufficient bilateral assistance cannot be obtained to complete the implementation of this initiative, we support the Fund’s selling a portion of its gold reserves for this purpose.

I would now like to turn to the subject of relations with the World Bank.

We appreciate the circumstances that over the past two years have led the Bank to make a number of administrative changes and to focus its efforts on improving project implementation, but we also note a reduction in the number of new commitments for FY 1997, and for the preceding year as well. It is disturbing that the decreased availability of new loans has hit particularly hard in regions that suffer from severe poverty, such as sub-Saharan Africa and South Asia, where World Bank and International Development Association (IDA) commitments fell significantly last year. It is also disturbing that the reduction in new commitments to the Arab world—over 40 percent—was larger than in any other region. We must therefore make exceptional efforts to increase the Bank's activities in these regions, to ensure its effective role in reducing poverty and supporting development efforts.

We look forward to implementing the reorganization program initiated by Mr. Wolfensohn within the framework of the Strategic Compact recently approved by the Bank's Board of Directors, which contains a number of basic reforms aimed at improving performance and enhancing the Bank's ability to serve its member countries more effectively and at lower cost.

I would also like to draw your attention to the positive accomplishments achieved by the World Bank Group over the past year. Foremost among them are the continued increase in drawings on IBRD and IDA credit facilities and the expanded activities of the IFC, along with its increased concern for the developmental effects of its investments and greater interest in investing in the small countries of Africa. We also welcome the increased number of guarantees provided by MIGA, and we support efforts to enhance its ability to provide even more of these guarantees, which encourage the flow of private capital. Moreover, we applaud the efforts made by Syria to normalize its financial relations with the World Bank and regain its right to avail itself of the Bank's services.

I would now like to discuss economic developments in the Arab world. The countries of this region witnessed a number of positive developments during 1996 and 1997, including significant improvements in most of the macroeconomic indicators, the renewed stability of economic conditions, and increased rates of growth. GDP grew by 4.5 percent in 1996 and is expected to achieve similar growth in 1997. This growth was also accompanied by an increase in real wages for the first time after four successive years of decline.

These positive developments also included an improvement in the general financial situation of both the oil and non-oil countries. Budget deficits in the region were reduced to about 2 percent of GDP in 1997, compared with 7 percent in the early 1990s. Inflation rates in the region fell to 8 percent in 1997, just half of the rate during the previous five years. The Arab countries also witnessed positive developments in their external performance, with the current account register showing a surplus for the first time since 1990. The external debt burden was also reduced in a number of countries.

The improvement in the region's economic performance is largely the result of the comprehensive financial and structural reforms implemented by a number of Arab countries, with the support and assistance of the World Bank and the IMF. The countries that adopted financial stability programs have begun to reap the benefits of reform. The Gulf countries have witnessed a significant improvement in their economic situation after several years of pursuing policies of financial reform.

Great efforts have also been made to revive the Palestinian economy and to build financial and economic institutions in Palestine, with the support of the World Bank, the IMF, and the donor countries. We applaud these valuable international efforts to assist the Palestine Authority in overcoming the difficult economic situation and poor standard of living in the Palestinian territories, but we regret that these efforts are faced with increasing obstacles caused by Israeli measures, which have stymied the efforts of the Palestinian people to develop their homeland and hindered the financial assistance provided by Arab and international donors, in addition to obstructing the pathway to peace in the Middle East. We therefore urge the World Bank Group, the IMF, all international organizations, and their member states to demand that the Israeli government release all financial assets belonging to the Palestine Authority, open the closed borders, and refrain from placing further obstacles to the development of the Palestinian economy.

Completion of structural reform aimed at increased economic liberalization is at the top of the agenda of the Arab countries. This is evident in the effective measures being taken by the countries of the region to implement privatization programs. It is also evident in the success that many of these countries have achieved in strengthening their banking and financial systems and freeing them from administrative constraints, in an attempt to stimulate financial mediation and improve the investment climate for the domestic and foreign private sectors. Also noteworthy are current structural reforms aimed at increasing production capacity and diversifying economic activity by providing new opportunities for the private sector. We hope that these important reforms will help solve the unemployment problem by creating new job opportunities that are sufficient to absorb the regions' steadily increasing labor market.

In view of the benefits of globalization and the need to increase their competitiveness, the Arab countries have taken measures to create a regional free trade zone, and members of the World Trade Organization have taken important steps to liberalize trade and open their markets to the outside world.

The marked improvement in the economic conditions of the Arab countries has led to increased capital flows in a number of them. We are hopeful that these countries will be able to attract further capital and increase their rates of investment. In this connection, an important step was taken in 1996 by the Arab development funds to encourage increased participation by the Arab private sector in reform and development activities, through new programs offered by the funds to provide financing for private sector projects.

The Arab states are well aware that, despite the improved economic performance of the region, they still have a long road to travel. The achievements of the past two years will serve as the cornerstone for future reforms. The Arab countries are also aware that improvements in the external environment are not sufficient to stimulate economic growth. Efforts must also be made to create domestic conditions that can help achieve sustainable high growth rates. Both elements are needed to create a climate that encourages domestic savings and productive investment, which in turn can help achieve high growth rates, provide increasing employment opportunities, and raise the standard of living of the region's population.

Before leaving our discussion of the Arab world, we must not forget that Libya continues to suffer from the sanctions and other constraints that have been placed upon it, and that other Arab countries are threatened with similar sanctions. It is our hope that these resolutions can be reconsidered in an objective light, in order to relieve the suffering of the people involved. We call for efforts to assist in the development of these countries by means that comply with the rules of international trade, to increase the flow of capital to these countries in accordance with the principles of the international financial institutions.

We urge the IMF and the World Bank to continue and intensify their efforts to provide financial support and technical assistance to Arab countries and their specialized agencies, thus enabling them to keep pace with the international economic system, in particular by providing the technical training necessary for modern economic management.

We welcome the approval by IMF members of the new SDR issue, and we urge member countries to complete in a timely manner the procedures for amending the Fund's Articles of Agreement in this respect.

With regard to the Eleventh General Review of the Quotas of IMF members, we feel that we must express our reservations concerning the approved method of distribution, which will lead to an overall reduction in the quotas of developing countries, just as these countries are assuming a greater role in the world economy.

We share the view expressed in your opening statement that the most important challenge facing the World Bank Group, the IMF, and all their member countries is the challenge of adapting to the new circumstances of a changing world. We welcome the efforts that have been made so far in this direction, and we look forward to further participation in helping our member states meet this challenge.

Statement by the Governor of the Bank for Ethiopia

Ato Sufian Ahmed

World Economic Outlook

Over the past three years, the increase in trade, financial flows, and exchanges of technology and information are factors that have created a more conducive environment for the expansion of the world economy. This process has generally led to encouraging performance and prospects for the developing countries as well as advanced economies and economies in transition. We are therefore encouraged to see that the macroeconomic and structural policies implemented in most of these countries have considerably eased inflationary expectations and reduced budgetary deficits, both of which have contributed to declining long-term interest rates as well as reduced erratic fluctuations in the exchange rates of the key currencies and further promoted international trade.

This favorable international economic environment has no doubt contributed to the progress made by the developing countries, which grew by about 6.5 percent in 1996. In Africa, economic reforms seem to be bearing fruit and have resulted in an average 4.8 percent growth rate in 1996, the highest in 20 years. Forecasts based on continuation of the adjustment policies and ongoing improvement in the international economic environment suggest that this rate of growth for the African countries is expected to rebound to 5 percent in 1998 after registering 3.7 percent in 1997.

As a number of studies have shown, Africa's economic performance remains below potential and is inadequate to reverse the trend in poverty. Africa must be competitive and produce more in order to achieve annual rates of growth above 7 percent. It is our view that it is only under such circumstances, with greater non-debt-creating capital inflows and strengthened human and institutional capacities, that Africa can meet the twofold challenge of improving the living conditions of its people and integrating into the world economy.

Africa and the Globalization of the Economy: Challenges and Opportunities

Meeting this twofold challenge is one of our key concerns, especially as we are aware of the marginalization of our continent in the current globalization of the economy. Indeed, based on the fact that globalization implies more dynamic international trade and capital flows, we must resolutely reverse, in international trade, the current decline in Africa's—and especially sub-Saharan Africa's—share, which stands below 2 percent. We must also considerably improve our saving and investment rates in comparison with those of other regions and must attract more foreign direct investment so as to raise its share of capital flows to the African region. Indeed, this should be possible as we have, through the implementation of structural adjustment programs, managed to keep our economies on the path of macroeconomic stability. Thus we have laid greater emphasis on market-based policies, redefining the role of the state in the economy and improving basic infrastructure. Our actions have also aimed at promoting the agricultural sector as well as the social and educational sectors, which, in our view, are the basis for sustained development. Furthermore, as we know that the sustainable growth of our economies and the improvement of the living standards of our populations are dependent on more efficient management of our resources, we are giving the highest priority to the issues of good governance, efficiency, and transparency in the management of public resources. However, all these efforts have not yet received the desired response from the international community.

We are determined to pursue our actions in all these areas, in spite of the limits of our current efforts. Consequently, we believe that the active support of the international community, and of the Bretton Woods institutions in particular, should enable us to achieve the objectives we have set. We hope that this support will form part of a mutually beneficial partnership, in which the advanced countries open their markets wider to our goods and services and in which our economic reforms are supported by concessional bilateral and multilateral financing. In this context, we are very much encouraged by the recent Group of Seven economic statement in Denver emphasizing the need for the international financial institutions to reinforce their efforts to support reforming sub-Saharan African countries in the areas of greater openness, regional integration, and wider participation in the world economy.

Resource Flows

We are cognizant of the need to accelerate the mobilization of our internal resources to promote higher investment rates. However, the contribution of additional external resources is also crucial in strengthening and improving the financing of our adjustment programs and projects in priority sectors. We believe that the international community has an important role to play in this process, particularly in helping our countries create conditions that favor the mobilization of external capital. We deeply regret the steady decline in official development assistance, which is marginally compensated for with private capital inflows. This decline makes it difficult for our countries to successfully complete the ambitious reform programs being implemented in the priority areas of our economies. As for International Development Association (IDA) resources, we are firmly committed to redoubling our efforts to ensure that these resources are mobilized and used effectively. In this regard, we must once again thank donors for their efforts to replenish IDA resources and their intention to explore long-term financing mechanisms for IDA.

Enhanced Structural Adjustment Facility

We reiterate our support for the Enhanced Structural Adjustment Facility (ESAF), which has thus far been very useful in supporting the adjustment programs of the low-income countries. While we are pleased with the broad consensus achieved in the international financial community in favor of continuing ESAF operations, we remain concerned about the uncertainties regarding its financing in the interim period (2000–2004). We, therefore, invite the IMF to do everything possible to ensure the adequate financing of this facility by the donor countries, especially at a time when the ESAF is called upon to play an additional role in providing debt relief within the framework of the Initiative for Heavily Indebted Poor Countries (HIPC Initiative). In this regard, we continue to be in favor of a partial sale of the IMF's gold holdings to supplement any shortfalls in contributions from the bilateral donors.

Private Capital Flows

We are determined to pursue the economic reforms needed to stimulate sustainable economic growth, with the private sector as the driving force. To achieve this key objective, we have undertaken to create or revitalize the financial markets and to introduce appropriate regulatory and legal frameworks. Our ambition is not only to mobilize domestic private capital, but also to have access to international capital markets. It is quite worrisome that capital flows to African countries remain inadequate. The international community should therefore support our efforts in this endeavor so that the African countries that have improved their macroeconomic environment may have voluntary access to the capital markets. Thus our countries would become less dependent on external aid. In addition, the World Bank, through the International Finance Corporation, should promote greater involvement of the domestic private sectors in the privatization process through "piggybacking" schemes. Furthermore, it should encourage the international private sector to participate in private investment financing, especially with regard to basic infrastructure.

The Debt Problem

The debt burden remains a significant constraint for the economic and social development of Africa, as it constitutes a substantial drain on our resources and limits the impact of our efforts to achieve our priority objectives. Indeed, in 1996, Africa's external debt increased to $320 billion, with a corresponding rise in the debt service to exports earnings ratio. Considering these figures, it is disturbing to note that Africa's debt burden continues to worsen, even though several countries have benefited from debt relief under several schemes (Toronto, Naples, IDA, etc.). It is also disturbing to note that multilateral debt rose to about 30 percent of total debt in 1996, compared with 16 percent in 1990. In this context, we consider that more viable solutions to our debt problem must be found urgently, so as to enable Africa to use its limited domestic resources for accelerating its development and its integration into the world economy. We appreciate the recent efforts of the international community and the Bretton Woods institutions to reduce the debt burden of some African countries under the HIPC Initiative. We also welcome the broadening of the eligibility criteria. However, we are still concerned by the three additional years required between the eligibility decision point and the completion point, during which a country is expected to demonstrate its commitment to its reform program, thus establishing a track record of reform. In our view, a rigid interpretation of what constitutes a good track record might defeat the very purpose of the initiative, which is to achieve a viable environment conducive to growth and development. We therefore ask for a reduction of the three-year period and greater flexibility in the implementation of this new initiative, so that it may indeed reduce significantly the external debt overhang of a large number of eligible countries. The Denver Declaration is, in this regard, very well appreciated, and we look forward to concrete actions by all creditors. Furthermore, for those countries that are ineligible for the HIPC Initiative and whose debt service continues to absorb too great a share of their resources, and here we refer especially to some middle-income countries, we urge the international community to consider the implementation of a debt relief mechanism that is adapted to their needs.

Capacity Building

Capacity building is the key to Africa's development. In this regard, we would like to pay particular tribute to the President of the World Bank for his exceptional commitment to this initiative. We appreciate the creation of a technical group for capacity building in the African region. We are pleased to observe that 12 capacity-building appraisals have been conducted and others are planned for the near future. All the workshops and seminars scheduled under this initiative have been held and have enabled African authorities to meet and discuss issues related to this topic and to consider practical solutions. The meetings also shed light on the goals and principles that should underlie this new African initiative—to build human and institutional capacities. We are also pleased to inform the assembly that we are in the process of putting in place national secretariats on capacity-building issues. The secretariats will be responsible for coordinating capacity-building issues and activities at the national level and will be the sole interlocutors with the donor community on these issues. We expect that a partnership group on capacity building in Africa and a capacity-building trust fund, which form the backbone of this initiative, will be created in the next few months. We appeal to all partners in development, including foundations and the private sector, to contribute as well. We are counting on the support and participation of the World Bank and the IMF in the mobilization of international financial and other assistance for the effective launching of the initiative. We wish to emphasize that our initiative is comprehensive and incorporates the activities of existing institutions, including those of the African Capacity-Building Foundation.

International Trade and Regional Integration

Notwithstanding the agreements reached within the World Trade Organization, export prospects remain uncertain for African countries. Our products still have limited access to international markets owing to the numerous barriers in those markets. However, we do recognize the positive aspects of the current Lomé agreements, and we are pleased with the draft treaty between the United States and Africa on trade and investment, which is currently being reviewed by Congress and also opens up new trade prospects for our countries. Africa must become more integrated into world trade. To this end, our countries have begun to take appropriate measures to eliminate obstacles to the movement of capital, goods, and people so as to accelerate cross-border investment. We urge the Bretton Woods institutions and the international community to support these efforts.

We are committed to pursuing the regional integration process under way with a view to enabling us to implement common projects, especially in the areas of basic infrastructure, information dissemination, and human resource development. While we know that, in all cases, we must first rely on our own resources, nonetheless, the international community has a role to play. In particular, we believe that the Bretton Woods institutions can create the necessary instruments to strengthen our subregional and regional economic integration so as to expand our limited domestic markets and create more viable economic entities.

STATEMENT BY THE GOVERNOR OF THE BANK FOR FIJI

James Ah Koy

It is an honor to attend the Fifty-Second Annual Meetings of the World Bank and the International Monetary Fund. On behalf of the government of the Republic of Fiji and its delegation, we extend warm greetings to the government and the people of China. We are privileged to be meeting here in Hong Kong, China, soon after the historic handover in July. My delegation and I are impressed by the excellent facilities and the warm hospitality of the Hong Kong community.

The robust growth in the industrial countries such as the United States, and recoveries in Japan and continental Europe, combined with low inflation, have provided a solid foundation for sustained expansion in developing countries. The continuing good performance of the global economy rests largely on the prudent management of industrial countries. I am encouraged by the commitment to suppress the threat of inflation with a proper balance between tight monetary policy and fiscal consolidation. However, if the economic dividends of this prudent management are to be shared by all, industrial countries must continue to resist the temptation to reverse trade liberalization. The rules of the General Agreement on Tariffs and Trade must be rules for everybody.

The developing countries, however, should not be under any illusion that the benefits of global expansion will accrue to countries automatically—they must be earned by hard work and disciplined policies. Without the right policies, some countries face the risk of being marginalized and will not share in the global expansion. To harness this growth opportunity, developing countries must play their part. Ongoing structural reforms to improve the allocation of resources and increase efficiency must continue. Macroeconomic stability can only be achieved through sound monetary policy and the political will to reduce the fiscal imbalance.

The World Bank and the International Monetary Fund must continue to recognize the extreme diversity among developing countries in size, economic endowment, and problems faced. The dynamic growth in Southeast Asia has been threatened by turmoil in the foreign exchange market at a time when we thought that the contagion effects of the Mexican crisis were well behind us. This brings into question the role of the Fund in its surveillance and the remedy it can offer. In my view, the Fund must urgently and seriously review its role of the custodian of exchange rate stability. The Fund, in its zeal for transparency and global integration, must take into account recent evidence that economic discipline, while essential, is not a sufficient condition for exchange rate stability. I therefore welcome the strengthening of the General Arrangements to Borrow, which can offer vital support in such crises. Whatever solution is preferred, a clear message from these crises is that the Fund must move decisively and immediately at the first sign of trouble.

At these annual meetings, we, the small members of the Bretton Woods institutions, have one of the few opportunities to express our views on specific problems and challenges that we face. While these may seem very minute to the international community, these problems are extremely real and imposing to us. We, therefore, urge the Bank and the Fund to continue to safeguard the evenhanded treatment of all member countries. The economic fate of the small South Pacific member countries, to a large extent, rests on our ability to expand our markets beyond the traditional bounds of Australia and New Zealand. Stability in Southeast Asia and the international exchange rate market is therefore very important to us.

We would also like to appeal to the Bank and the Fund to adopt a country-specific approach to the needs of the developing member countries. As a small nation, Fiji fully embraces the policy of trade liberalization. However, in embarking on this process, it is essential that we give our local industries the tools and the infrastructure to allow them to compete on a level playing field with our bigger and established competitors. This cannot be done successfully overnight. The pace and sequence of trade liberalization must be consistent with other micro reforms in the country. Otherwise, the only beneficiaries of our accelerated trade reforms are our major trading partners, at a cost to us of high unemployment.

The recent exchange crisis in Southeast Asia has placed considerable attention on fixed exchange rate arrangement and capital account convertibility—issues that are very important to small countries like Fiji with narrow domestic markets and export base. The currency stability and the inflation anchor that a fixed arrangement offers has worked well for us. However, we realize that we need to regularly review this arrangement, and the current discussion of exit policy in the Fund will provide some guidance to our future direction. At the same time, we urge the Fund, in its discussion of capital account convertibility, to consider carefully the susceptibility of small developing member countries, and grant transitional conditions to them.

I am happy to report that Fiji's monetary policy has kept inflation contained at about 3 percent and is likely to stay low over the coming years. External financial stability has also been maintained. My government is committed to restoring fiscal balance by the year 2000. We fully realize that, to lift our growth path, Fiji needs to better harness its economic potential, raise the level of investment, and provide sufficient resources to the private sector to spearhead economic expansion. We will continue to look to the Fund and the Bank to assist us in facing these daunting challenges and, in this regard, we particularly support the initiative to involve the private sector in infrastructural development.

The major single challenge that small Pacific islands face is the potential loss of preferential trade arrangements to Europe under the Lomé Agreement and to Australia and New Zealand under the South Pacific Regional Trade Economic Cooperation Agreement. Therefore, we appeal to the international community for sufficient time and resources to make the necessary transition, and to the multilateral institutions for assistance in this endeavor. Needless to say, the Fund and the Bank need to be furnished with adequate resources to meet the growing demand of member countries. Therefore, we fully applaud the decisions to increase the Fund’s quota and to replenish International Development Association resources.

Pacific islands are isolated geographically from the major markets, and high transport costs reduce the competitiveness of our exports. We are also isolated in the context of information, with technology transfer slow and uneven. We import a large part of our needs and rely heavily on the export of a few major commodities. We are particularly vulnerable to fluctuations in the terms of trade and supply shocks caused by cyclones and other natural disasters. Being small, with relatively underdeveloped financial markets, we are also exposed to large and irregular capital flows in response to shifts in foreign policies and investor sentiment.

The message that comes out loud and clear is that we need to be competitive if we are to survive in this new world order of globalization. To be competitive, we will need to develop: an enabling social and physical infrastructure; a healthy, well-educated population; a transparent set of property rights; a well-functioning legal system; an efficient system of transportation and communication; and small, but efficient administrative systems. These require resources and skills that we do not possess. Our future needs for Bank and Fund assistance will continue to be for infrastructure and human resource development, institutional strengthening, and economic policy advice.

In this regard, Fiji is indebted to the Bank’s and Fund’s past and ongoing assistance to the region, and to the country. In particular, we have found the Pacific Technical Assistance Center very useful, and we are thankful to the United Nations Development Programme, the Fund, and other donor countries for their indication of support to the center for another three-year term.

I conclude by wishing the Bank and the Fund well in their next year of operation.

Statement by the Governor of the Bank for Finland

Sauli Niinistö

On behalf of the Nordic countries—Denmark, Finland, Iceland, Norway, and Sweden—I would like to express my appreciation to the people and governments of the People's Republic of China and Hong Kong for their generosity in hosting the Annual Meetings of the World Bank Group and the International Monetary Fund. The economic and institutional setup of Hong Kong has led to remarkable economic performance in the past. On this occasion, I would like to extend my best wishes also for the future of Hong Kong.

World Economy

The world economy continues to grow at a steady pace with low inflation. I note with particular satisfaction that recent estimates indicate that 5 out of 20 of the world's fastest-growing economies, likely to grow more than 6 percent in 1997, are located in Africa. In the transition countries, the fast reformers are today attracting significant amounts of direct foreign capital, and the private sector in those countries counts for more than two-thirds of GDP. It is evident that strong reform policies show tangible results. The World Bank Group should continue to support such efforts.

Looking ahead, the overall picture for growth is expected to remain favorable. Yet demanding challenges remain. The policy track record and economic performance in developing countries, as well as in the transition countries, have begun to differ significantly. We witness growing inequities both within and between countries, increased national vulnerability and global environmental degradation. Our challenge is how we seize the positive opportunities and curb the negative impacts of the process of economic globalization. This is a cause for deep concern and demands special attention. The Bank Group can and should play a role in this process.

Private Capital Flows and Financial Sector Development

The continuously increasing private financial flows now constitute more than four-fifths of the international capital flows to the developing world. While still heavily concentrated on some limited number of countries, new countries could seize the opportunity of utilizing these flows by creating a more hospitable environment for private sector participation. We should actively foster private sector–led development while ensuring that the resulting growth reaches all segments of society.

In many of the most successful developing countries, a vibrant private sector has been the engine of growth, producing job opportunities and generating incomes. Increased private sector engagement in the economy broadens the tax base and releases public resources. This contributes to macroeconomic stability and allows increased social expenditures.

A challenge for the World Bank Group is to enhance private sector development by helping to catalyze private capital flows and to support governments in establishing an enabling environment needed for private involvement. Two important elements in such a strategy are institutional development and increased use of guarantees. This should be done in close collaboration with the private sector entrepreneurs and partner governments.

An effective financial intermediation lies at the core of mobilization of resources and a well-functioning private sector. Recent turbulence in financial markets, particularly in Asia, is a reminder that the financial sector remains highly sensitive to imbalances, sometimes with severe consequences for the people and societies involved. In an interdependent world, such problems are spreading rapidly.

Concerted and systematic international efforts are needed to restore public confidence and to consolidate financial sectors nurturing growth and development. We urge the World Bank Group to give assistance to its member countries in matters related to development of the financial sector. The Nordic countries welcome efforts by the Bank and the Fund to increase collaboration and also to clarify further the division of labor in this field.

Role of the Public Sector as a Facilitator

The state has a crucial role in providing the overall framework for development, including systems of law, education, health, and regulatory structures. A prerequisite for favorable private sector development is an effective public sector that complements the private sector by providing a framework conducive to sustainable economic and social development. A well-balanced division of labor between public and private sector responsibilities guarantees the best outcome. We welcome the emphasis on the role of the state in the *World Development Report 1997*. We encourage the Bank Group to continue to help countries in speeding up liberalization of national economies and in reducing public sector involvement in commodity producing activities.

Good governance is central for economic efficiency, growth, and sustainable development. We warmly welcome recent initiatives by the Bank and IMF to support good governance and guard against corruption. The fight against corruption to undercut its adverse effects should be intensified. Corruption must be taken into account in lending decisions. Credibility, transparency, and accountability are important underpinnings of all-out development efforts.

Official Development Assistance (ODA) and Initiative for Heavily Indebted Poor Countries (HIPC Initiative)

Despite the propitious development of private international capital flows, the majority of the poorest countries are still primarily dependent on the concessional aid resources. To take full advantage of the increased private capital flows in the future, they will continue to require official external assistance to buttress ongoing reform processes and to support investments needed for sustainable development. We are deeply concerned about the declining trend of official development assistance (ODA), which needs to be reversed.

Scarce ODA resources should be used effectively. We need to be more selective and performance based. All the partners should strive for improving the allocation of concessional flows by targeting, to a larger extent, recipients with firm commitment to reforms. This will increase the likelihood of sustainable development impacts and also backup for future allocations.

As strong supporters of the HIPC Initiative, we are deeply concerned at disagreements over the initiative's costs and a general unwillingness to contribute, which are shifting focus away from the needs of the eligible countries. Reaching debt sustainability is crucial for leading the way to more sustainable overall development.

Development in the Transition Economies

Let me now touch upon more closely the recent developments in the transition countries. In the advanced transition economies, the progress already achieved in macroeconomic stabilization and structural change is already forming the basis for resumed economic growth. For the applicant transition countries, the accession to the European Union is posing several challenges in the coming years. Apart from macroeconomic convergence, all member candidates need to pursue further structural and institutional adjustments in order to harmonize current practices with future requirements. The Bank is in a unique position to help these countries in this process in close cooperation with the European Union.

Russia is at a critical juncture in its economic transformation process. We commend the Bank's commitment to its assistance for Russia. Strengthening the rule of law in the legal and regulatory systems, especially in areas relating to the financial sector, property rights, and competition, is necessary.

There is a necessity to pursue privatization further in every transition country. However, at the same time, the World Bank should also try to moderate the negative aspects transition may have on socially vulnerable groups by establishing viable social safety nets, which must be well designed in order to meet the needs of those who really need support from the society. The social sector loans recently approved by the Bank are necessary and welcome. The environmental situation in the transition economies gives rise to a deep concern. This is a vast task, and all the international financial institutions must work together in this area. We wish the Bank would also take a more active role in the environmental sector in Russia, where small-scale projects have proven to be most effective.

Strategic Compact

The Strategic Compact acknowledges the fundamental changes that have occurred worldwide. It is the Bank's response to the abovementioned challenges. I commend President Wolfensohn and his staff for their commitment to this reform. The Nordic countries support the renewal process. We expect to see it leading to a more flexible and results-oriented institution that remains dedicated to the fundamental objective of poverty alleviation through sustainable growth and investment in people.

The true challenge now, both for the institution and the shareholders, lies in translating these commitments into proper actions. The levels of ambition and expectation built into the process are highly demanding. An intense monitoring of the progress is a key factor to its success. The vision of what the Bank Group wants to be in the beginning of the new millennium is clear: the most effective global financial and development institution for fighting poverty. I think we all share this aspiration.

Statement by the Alternate Governor of the Fund for France

Jean-Claude Trichet

The Annual Meetings in Hong Kong will long be remembered by our institutions as being among the most successful. The Interim Committee agreement on a significant increase in Fund quotas and a one-time allocation of SDRs to end the problem of inequity, on the one hand, and the Development Committee's support for the IMF and World Bank action plan to promote good governance and combat corruption, on the other, stand as significant advances. Another important achievement of this meeting, in my view, is the agreement to draft an amendment of the Fund's Articles of Agreement to promote the orderly liberalization of capital movements.

The objective of achieving free capital movements throughout the world is quite ambitious. As demonstrated by the recent financial crisis in

Asia, such freedom creates new risks and imposes new forms of discipline. It is therefore useful to reflect on certain lessons from that crisis, to be able to determine precisely what the concept—new to our discussions—of orderly liberalization means. I will highlight two aspects related to market information and the pivotal role of the IMF.

As a result of the strengthening of surveillance following the Mexican crisis, the IMF anticipated the crisis in Thailand, pointing out to anyone willing to listen that certain external deficits had become unsustainable and that the obstinate defense of exchange rates no longer based on sound economic policies was dangerous and bound to fail. It has been asked whether a more public expression of the Fund's concerns would have been appropriate. As far as I am concerned, I consider that the Fund has done well. But I agree that public awareness of the IMF's independent and informed judgment, as is done for industrial countries with each report on the *World Economic Outlook,* may usefully contribute to the proper functioning of markets.

The second lesson is that only an institution with universal scope, such as the IMF, is capable of fulfilling all of the conditions necessary for handling crises in a globalized economy. The needed financing can be mobilized only on the basis of member countries' confidence in the firm and objective IMF conditionality. Nothing could be more dangerous than organizing financial support without backing it with the discipline provided by the IMF, be it in respect of governments or of markets. Taking Thailand as an example, I would reiterate that it is essential that commitments entered into with the IMF be strictly honored on time and that the financial sector restructuring currently being negotiated with the World Bank result in losses being shared equally by all improvident creditors.

Even more important is that, to be successful, the liberalization of capital movements must proceed in an orderly fashion. Capital movements enter and exit freely. A government cannot applaud inflows that enable it to finance accelerated growth and then denounce outflows when an excessive external deficit or economic policy blunders drive investors away.

The fundamental purpose of an amendment of the Articles is the universal recognition that the freedom to save and invest provides the conditions for sustained growth and therefore for greater wealth, for both providers and recipients of capital flows. From this perspective, the prosperity of Hong Kong—an open economy if ever there was one—and China's leap forward since the adoption of the open-door policy are more eloquent than any demonstration.

The first condition for successful liberalization is irreversible acceptance by each country of the discipline required by openness, the first of which is macroeconomic discipline. Reversals are always costly for countries that decide on such a course of action. Lost confidence is only slowly regained. The definition of a liberalization program should explicitly aim at the irreversibility of measures taken, although it is impossible to rule out imposing exceptional, limited controls in the event of a setback.

In this connection, the preparatory efforts have quite rightly emphasized the necessity of a pragmatic, gradual approach that allows for transitions. I favor this caution and believe that each country should determine what it can do, based on the stage of development of its economy. However, I would also remind you that hesitating too long can be costly, as it entails the risk of marginalization from the increasingly interrelated international flows in goods, services, and capital, and thus of missing out on opportunities for growth. For some countries, acting in time means waiting until conditions are right; for others, it means moving faster.

Another aspect of this orderly progression is the balance between internal and external liberalization. We all stress—and the IMF will never do it too much—the importance of strengthening the safety of the financial sector and the reliability of prudential control systems. Clearly, the IMF will play a decisive role in detecting potential crises through its surveillance, and in disseminating and monitoring the implementation of the core prudential principles formulated by the Basle Committee in close conjunction with the banking supervisors of emerging and transition countries. It is also particularly welcome that the World Bank is committed to giving clear priority in its activities to the restructuring of financial sectors.

Although it is the most important, the prudential aspect is not the only concern. Three examples come to mind: the need for a vigilant conduct of monetary policy, particularly in the occurrence of excessive short-term capital inflows denominated in foreign currencies; increased competition among banks, specifically promoted by greater openness to foreign banks; and appropriate surveillance and regulation of domestic capital markets.

Finally, liberalization should apply evenly to all capital movements. I have some reservations about the arguments suggesting that liberalization of inward direct investment should be excluded from the mandate of the IMF on the grounds that non-economic considerations are frequently involved in the decision to maintain restrictions. Foreign direct investment makes an essential contribution to growth and balance of payments stability. Excluding such capital flow and having the IMF focus narrowly on achieving freedom of financial and short-term capital movements would not be consistent with our efforts to pursue an orderly liberalization. Naturally, the IMF should acknowledge the legitimacy of restrictions specific in their purpose, limited in their impact, and motivated by considerations of national interest unrelated to the conduct of economic policy.

I now turn to the creation of the euro, an event that will be of the utmost importance both for European countries and the international monetary system. I stress that France is firmly committed to the achievement of European Economic and Monetary Union (EMU).

A few days ago, in Mondorf, during an informal meeting of the Economic and Financial Council of the European Union, the Ministers of Finance and Governors sent a clear signal of their determination. They announced that the list of countries and bilateral conversion rates, which will enter into force on January 1, 1999, will be made known on a single date next spring. This is an important decision that was well understood in Europe and throughout the world.

Economic and Monetary Union will be achieved in accordance with the criteria and the timetable set forth in the treaty. Accordingly, the convergence of many European countries toward the performance of the best among them warrants special mention.

Collective progress in the area of monetary stability, the curbing of inflation, the lowering of long-term interest rates, and the reduction of government deficits has been substantial. As far as France is concerned, I would particularly like to mention our long-term interest rates, which are among the lowest in the European Union, our control over inflation, and the orderly reduction of budget deficits. After 1999, the EMU should—and will—serve as an area of stability.

A sound and stable euro will guarantee that. The citizens of Europe want a single currency that is credible and that inspires trust. Confidence in the single currency in Europe and worldwide will enable Europe to benefit from the best financing conditions. This confidence will be reinforced by the independence of the European System of Central Banks, which will fully benefit from the strength of the most credible national central banks of the countries using the euro, whose legacy it will inherit.

Fiscal stability will be ensured by the determination of governments to consolidate public deficits on a sustainable basis in the context of the Stability and Growth Pact agreed in Amsterdam in June 1997.

Lastly, the strengthened coordination of economic policies decided upon in Amsterdam will clearly benefit integration of the euro zone.

Thus, EMU has the potential to promote confidence, growth, and employment. Following a French initiative, a summit on employment in November 1997 was announced in Amsterdam, as employment is one of France's primary concerns. However, growth alone cannot bring about a sufficient reduction in unemployment if we fail to implement the necessary structural reforms, particularly with respect to adapting training to the needs of the economy. This is an important task for our country, as it is for most European countries.

Finally, let me commend the World Bank and the IMF for successfully implementing the initiative for reducing the debt of the heavily indebted poor countries approved last year, and for their productive cooperation with the Paris Club. The main challenge now is for this initiative to be implemented consistently, both by eligible countries—which should hasten to conclude and implement their adjustment and reform programs—and by the institutions, through the effective mobilization of financial support.

In this regard, France is concerned by the temptation to offer verbal support without any financial participation, which continues to exist here and there, and by the persistent silence of certain countries concerning their contribution to the financing of the self-sustained Enhanced Structural Adjustment Facility (ESAF) and the IMF contribution to the Initiative for Heavily Indebted Poor Countries. We should therefore refrain from making new promises before securing the financing of our commitments.

This does not mean that further progress is impossible. I particularly hope that other creditors will forgive development assistance debt, as France and other European countries have been doing for several years and as the United Kingdom decided to do, and that the World Bank will explicitly consider ways of helping the African Development Bank contribute to the debt relief initiative.

Statement by the Alternate Governor of the Fund for Germany

Theo Waigel

First of all, I would like to thank the government of the People's Republic of China and the government of the Special Administrative Region of Hong Kong for an excellent organization of this year's Annual Meetings and for their warm hospitality.

Increasing interdependence of our economies, buoyant international trade and the integration of our capital markets are essential prerequisites for increasing global prosperity. The spread of globalization has enabled many countries to gain access for the first time to international capital and product markets.

But intense global competition confronts our economies and our economic and fiscal policies with new challenges. If economic and fiscal policies are out of line with economic fundamentals, and if policies remain unadjusted, the markets will respond by reassessing credit risk and possibly by massively withdrawing financial resources.

Delayed implementation of exchange rate policy adjustments in combination with other risk factors, such as excessive and short-term foreign currency debt and a high and potentially rising current account deficit, will inevitably be followed by a loss of growth and jobs. This has been clearly evident in some Southeast Asian countries during the past weeks and months. It is now important for those countries to implement the necessary reforms and make up the international loss of confidence.

We must not conclude from the currency turbulence in parts of this region that capital transactions should be more strongly regulated or controlled. Rather, free international capital movements are a central element of an efficient resource allocation and therefore a precondition for rising global prosperity.

Experience in many industrial economies and in some emerging countries as well has shown that liberalization must go hand in hand with the establishment of stable financial market structures. The IMF and the World Bank can—and in fact must—assume a key role in these endeavors.

Against the background of globalization, it is appropriate for the IMF to be given a new, extended mandate to include promoting the liberalization of capital transactions. Extending and thus modernizing the IMF's Articles of Agreement is essential to ensure that the IMF is able to make an effective contribution in this area of central significance for the efficiency of the world economic and monetary system.

Recent events in Southeast Asia have shown that the classic role of the IMF should continue to be the central pillar of its activity. In particular, this includes the surveillance of economic policies in member countries to prevent crises and the temporary provision of conditional financial resources in the event of balance of payments need. Therefore, I welcome the consensus we reached here in Hong Kong on increasing the Fund's resources. I am grateful for the spirit of cooperation that has prevailed among IMF members. I would also like to thank Michel Camdessus.

But interdependent markets also call for enhanced economic policy surveillance by the IMF. This purpose is served by setting up standards for the publication of economic statistics, which in turn will provide a basis for intensifying surveillance in the interest of transparency.

The IMF and the World Bank perform complementary activities. The adoption of the World Bank reform program—the Strategic Compact—in the past year was an important landmark on the road to reorganization. I would like to congratulate President Wolfensohn for that. The reform process now set in train aims generally to make the World Bank more flexible, more responsive to customer needs, and more efficient and to bring its range of services more closely into line with its development policy mandate.

In this way, the World Bank is responding both to the new global economic and social challenges in its environment and to the growing diversity in the needs of its customers. The reforms envisaged at the World Bank will improve its efficiency in promoting sustainable development, especially in the poorest countries.

The International Development Association (IDA) is the central global instrument in the fight against poverty and thus has a key role to play in Africa. The poorest countries of the world need adequate access to aid on concessionary terms to facilitate their successful integration into the global economy, which would be reflected in improved living standards for their peoples. The development policy mandate of IDA and its achievements to date should motivate all donor countries to honor their commitments and to put IDA finance on a sound footing. This is also true for the African Development Fund.

Finally, a word on the realization of European Economic and Monetary Union (EMU). Economic convergence has made further progress. The inflation rate in the European Union (EU) has been cut by half over the past few years and now stands at an average of about 2 percent for all member states. This is the lowest in 35 years. Interest rate differentials have fallen to an all-time low. Further progress has also been made on fiscal consolidation. As long as the EU member states do their homework thoroughly, EMU will start on time, on January 1, 1999.

Europe wants to see a strong and stable euro and has taken decisive steps toward this. A principal commitment of the future European Central Bank will be to maintain price stability. Its independence is guaranteed under international law. The economic policy pursued by member states in the EMU will remain the responsibility of the respective governments, but the coordination of these policies will be intensified to make sure that they are attuned to the stability objective of EMU.

Maintaining stability is also the objective of the Stability and Growth Pact we Europeans concluded a few months ago in Amsterdam on the level of heads of state or government. The pact requires member states to pursue stability-oriented fiscal policies and maintain a budget “close to balance or in surplus.” In any case, budget deficits in excess of 3 percent of GDP have to be avoided. Europe’s future currency, the euro, will be no less stable than other key currencies. A strong and stable euro is a further contribution by Europe to maintaining the stability of the international monetary system and to promoting prosperity throughout the world economy.

Statement by the Governor of the Bank for Greece

Yannos Papantoniou

In 1997 the global economy is characterized by rapid growth led by the U.S. economic recovery, a stronger commitment towards price stability, and an intensification of the fiscal consolidation process in many countries. The recovery in Europe and in the transition countries, combined with a growing number of successful economies in the developing world, signal that the current expansion of world output could be sustainable.

The emergence of a new international currency, the euro, is expected to have worldwide effects. A strong and stable euro may match the role of the U.S. dollar as a means of payment and an international asset. Moreover, it will create a more stable financial climate in Europe that will have a positive impact on international financial markets.

The creation of the euro area will contribute to sustainable growth in Europe. Prudent fiscal policies, a credible commitment to price stability, and the elimination of the risk premia associated with multiple EU currencies will tend to lower real interest rates and promote investment.

In contrast to this positive global outlook stands the unsatisfactory employment performance in Europe. Tackling Europe's unemployment can be a critical factor for the success of European Economic and Monetary Union. The forthcoming special meeting of the European Council in Luxembourg is expected to give a new impetus in the fight against unemployment.

Let me now turn to recent economic developments in Greece. In the past four years, the Greek economy has shown substantial progress on many fronts. The fiscal deficit has been reduced by about 10 percentage points of GDP since 1993, the debt-to-GDP ratio has been stabilized, while inflation has fallen from 14.3 percent in 1993 to an expected 5.7 percent in 1997. At the same time, GDP growth has gradually accelerated to 2.6 percent in 1996 and an estimated 3.5 percent in 1997, from minus 1 percent in 1993. The rise in private capital spending has more than compensated the fall in demand due to fiscal consolidation. The major forces that have created this virtuous cycle have been increased policy credibility, a considerable boost in business confidence, a significant fall in real lending rates, and an expansionary public investment program, which is partly supported by European Union funds.

The new government, which was formed after the September 1996 general elections, has decided to accelerate fiscal consolidation so that Greece can achieve the Maastricht Treaty convergence criteria by 1998 or 1999 and, hence, participate in the third stage of EMU by the year 2001. The 1997 budget is an ambitious one, aimed at bringing the general government deficit-to-GDP ratio down to 4.2 percent from 7.5 percent in 1996. Preliminary results in the first seven months of the year suggest that the budget is on track.

The restrictive stance of fiscal, monetary, and exchange rate policies has contributed to the deceleration of inflation. The exchange rate policy pursued, while playing an important role in combating inflation, did not have adverse effects on competitiveness on account of the substantial fall in interest rates and firms' financial costs as well as the limited rise in raw material prices. The sustained profitability of the business sector in recent years, which mainly produces traded goods, supports this view. The "stable drachma" policy remains a constant parameter in our economic strategy.

Good economic performance since the beginning of the year has produced buoyancy in capital and money markets. The Athens Stock Exchange Index rose by more than 70 percent since the beginning of the year. Interest rates are falling faster than forecast in the budget. Three-, five- and seven-year fixed-rate bonds, index-linked bonds, and zero coupon bonds have been issued for the first time in Greece. The result was judged by markets as a success.

Apart from macroeconomic policies pursued, the government has put more emphasis on structural policies. Recent legislation—which gives greater independence to the management of public corporations, the partial privatization of the Hellenic Telecommunications Company (OTE), the selling of certain industrial firms, the creation of the Hellenic Investment Center to facilitate foreign direct investment, legislation concerning new labor market policies, and the acceleration of the absorption of European Union structural funds—is expected to produce favorable results in the coming years. The focus of structural policies is on the following:

- partial privatization of profitable public corporations;
- labor market and pension system reform based on social consensus;
- granting statutory independence to the Bank of Greece;
- creating new schemes for the financing of public works, with increased participation of the private sector;
- rigorous application of recently adopted legislation for curbing public expenditure and improving the efficiency of the public sector;
- introducing legislation to further modernize capital and money markets and strengthen the supervisory powers of the Capital Market Committee; and
- restructuring the portfolios of the large state-controlled banks.

Greece's economic prospects are further enhanced by the opening of trade and investment opportunities as a result of the transition of its Balkan and Black Sea neighbors to democracy and market economies. The Greek government actively promotes increased international cooperation by encouraging the creation of joint ventures aimed at improving economic structures in the region.

The 1998 budget is now under consideration. The government aims at a public deficit-to-GDP ratio of less than 3 percent, which will satisfy the Maastricht Treaty criterion for entering the European Economic and Monetary Union. Tight budget, incomes, and monetary policies ensure the continuation of nominal convergence, while continued investment expansion—both private and public—partly financed by the European Union, and the pursuit of structural policies lay the basis for robust growth of output for the years to come.

Statement by the Governor of the Fund for Iceland

Birgir Ísl. Gunnarsson

I have the honor of addressing this meeting on behalf of the Nordic and Baltic countries—Denmark, Finland, Iceland, Norway, Sweden, Estonia, Latvia and Lithuania—on matters relating to the International Monetary Fund. At the outset I would like to thank the Chinese government for the hospitality extended to us here in Hong Kong. Following the return of Hong Kong to China earlier this year, I would also like to use this opportunity to extend my best wishes for the future of Hong Kong and of China in general, both of which have shown an impressive economic performance in previous years.

World Economic Outlook

The Nordic and Baltic countries support stability-oriented economic policies conducive to growth and expansion of world trade. In addition to sound public finances, ongoing sweeping changes in many parts of the world that contribute to this effect are increased market orientation, dismantling of trade barriers, liberalization of capital flows, and privatization of public enterprises. All of these measures have provided tangible results, as evidenced by the healthy expansion in the world economy and the strong rise in the volume of world trade. Currently, the world economy is expanding at the strongest pace in a decade, with the trend growth rate in the world economy about 4½ percent while global inflation remains subdued. It is encouraging that the expansion is firmly underpinned by strong growth in various parts of the world.

While several advanced economies are operating at relatively high capacity, the slow growth of many economies of continental Europe is far from satisfactory and suggests the need for more vigorous structural reform policies. Moreover, in previous years a slowdown, and even recessions, have followed episodes of relatively rapid growth in many countries. Given that experience, the overall current positive developments in the world economy create the challenge of sustaining the healthy noninflationary growth of the recent past.

In the advanced economies, the current developments have been largely characterized by the high degree of price stability that remains an impressive achievement shared by most of these countries. Indeed, the low inflation levels and widespread commitment to stable prices count among the major factors that contribute to the solid economic growth and the favorable prospects of sustaining current expansion in the period ahead. In the economic outlook, however, there are various elements of concern, among them the risk of overheating in some countries. It is vital that we stay on guard to counter the possibility of inflation rising again. We must be prepared to use the policy measures available to us in this regard.

It is encouraging that in the developing countries real GDP growth is expected to remain relatively buoyant at about 6½ percent in 1997, with similar growth being projected for the coming year. Macroeconomic stability and prompt implementation of necessary reforms are fundamental to sustain this improvement in the period ahead and to enhance the generally positive long-term prospects for these countries. The growing number of successful economies in the developing world is opening new markets and creating increased production capacities.

In countries in transition, as well as in developing countries, it is clear that many challenges remain to be addressed to safeguard and further extend the progress that has been achieved. The experience of several countries in transition suggests that the process of turning centrally planned systems into market economies is providing successful results. This is particularly evident in the countries that have pursued the most comprehensive stabilization and reform policies. These countries are increasingly being reintegrated into the world economic and financial system. The less advanced transition economies need to increase their efforts and embark on comprehensive reform programs that include the establishment of market economy institutions and the development of financial markets capable of efficiently channeling funds into productive investments.

In regard to general policy formulation in all countries, there is no alternative to the policies that have proven most successful and conducive to sustainable growth. We need a balanced mix of monetary and fiscal policies to ensure economic stability and growth in the long term. With monetary policy directed at price stability, the design of sound fiscal policies must take into account the need to foster savings as a prerequisite for investment and growth. We need structural policies to free up economic resources bound by restrictions in the form of excessive regulations and impediments to trade and capital flows. We need comprehensive labor market reform that, together with efforts in the field of education and training, can facilitate new economic dynamism and tackle the unemployment problem. In order to safeguard long-term growth, we need environmentally sound policies. We need free and open markets that allow developing countries and transition economies to earn their way to economic prosperity through a vibrant world trade that is beneficial to all countries.

World Monetary System

In light of imminent Economic and Monetary Union (EMU) in Europe, with one single currency replacing various national currencies, the world monetary system is at an important juncture. Replacement of the currencies of several economies of this size and state of development with a single common currency is unprecedented in history. With its systemic consequences, EMU will create new challenges for the world monetary system. But while EMU will be a major change it will not be a sudden change. The establishment of the common currency will reflect a process of four decades within Europe characterized by strengthening economic and monetary ties.

For participating countries, EMU will represent a change in the monetary policy regime where national monetary policies will be replaced by a policy attuned to conditions throughout the euro area. The effects of EMU on the world economy will depend on the economic performance in Europe and the extent to which the euro is used in international transactions. Given the scope of the changes that the EMU entails, it is important that a smooth transition to the new monetary regime be effected.

Role of the Fund

The International Monetary Fund plays a vital and central role in the surveillance of the global economy and world monetary issues. Given the need to efficiently detect problems in the world economy and provide an early warning of unfavorable developments to facilitate prompt policy response, I would like to underline the importance of the surveillance functions of the Fund in regard to the world economy as well as surveillance of individual member countries' economic policies. The recent market turbulence in Southeast Asia has highlighted the importance of strong and confidence-building macroeconomic and structural policies and early policy action when imbalances build up. The Fund has an important surveillance role in that regard, but the ultimate responsibility lies with the countries themselves. The Fund also has a vital role to play as a catalyst for financial flows to developing countries and transition economies. In this function, the Fund must continue to build on the basis of established practices, with strict conditionality and taking into account the revolving character of its resources.

We must, at all times, ensure that the Fund has the capacity necessary to carry out the functions specified in its mandate. Thus, I welcome the agreement by the Executive Board on the quota increase. I also welcome yesterday's unanimous decision on the special one-time SDR allocation.

The increasingly open and liberal system of capital movements is highly beneficial to the world economy. Capital liberalization, backed by sound macroeconomic and structural policies, is conducive to investment and growth. Future positive developments of global financial markets and the prevention of market turmoil would be enhanced by an international agreement to promote orderly capital liberalization. Thus, we support an amendment of the Articles of Agreement in order to extend the Fund's mandate to cover capital movements.

I would also like to welcome the launching of the Initiative for Heavily Indebted Poor Countries. It is essential that this one-time effort be further secured through adequate financing based on the principle of fair burden sharing.

The Fund has a central role to play to strengthen future prospects for growth and employment in all its member countries, based on the agreed principles of the 1996 Interim Committee Declaration on Partnership for Sustainable Global Growth. Looking ahead, further economic cooperation and policy coordination form the basis for meeting the future challenges in the world economy.

Statement by the Alternate Governor of the Fund for India

Chakravarthy Rangarajan

The Annual Meetings of the World Bank Group and the International Monetary Fund at Hong Kong, China are of historic significance, coming as they do immediately after the unification of Hong Kong with China. In many ways, Hong Kong epitomizes the tremendous potential for economic development through openness to foreign trade and investment within a framework of a sound regulatory environment. Hong Kong has a fairly large community of Indian origin that has contributed to Hong Kong's development for more than a century, and I am sure it will continue to do so in future. We thank the Chinese authorities for the excellent arrangements and warm hospitality.

World growth has continued to be strong, thanks in part to the high growth of developing countries and the prolonged boom of the U.S. economy. Inflation has also remained low. However, there are some reasons for concern. World trade growth decelerated significantly in 1996, with sharp slowdown in export growth in many Asian countries. The medium-term outlook for developing country growth is less buoyant than in the spring of this year. There is, therefore, a need for concerted policy action to reverse any incipient sign of deceleration of growth in these countries. In this context, it is essential to encourage rapid recovery through strengthening of an open, nondiscriminatory multilateral trading system operating within the World Trade Organization framework. Along with free trade and buoyant private capital flows, there is a need to augment flows of official development assistance, which remains crucial for the development of poorer countries with limited access to private capital markets.

The crisis in some East Asian currencies has been an important feature of the global economy in the recent months. Led by the IMF, the swift action on the part of the international community in putting together a rescue package has helped to reduce the costs of the crisis and contain the spillover effects on other countries. It is clear from these developments that there can be no substitute for prudent macroeconomic policies, effective economic reforms, and strong domestic financial systems to facilitate growth with price stability and orderly external payments conditions. It is essentially through such a strategy that countries can avoid currency crises and also lay the foundation for the rapid and sustained development that is necessary for raising general living standards and alleviating poverty.

The accelerating pace of globalization and integration of markets requires strengthening of institutions, at both the national and international levels. At the international level, policy coordination is needed to strengthen economic linkages. Multilateral institutions must help promote an environment that is conducive to worldwide prosperity. These institutions, therefore, need to be strengthened, with decision making in these institutions being made more transparent and democratic. The conclusion of the Eleventh General Review of Quotas has given the Fund extra strength, although regrettably the voting share of developing countries has declined in the process. There is a clear need to review the formulas for quota calculations before the next Quota Review so that the fast-growing developing economies get their due share. The one-time special allocation of SDRs is a reflection of international goodwill, since it will help those members that could not participate in previous allocations while at the same time ensuring some allocation to every country.

We fully support the proposal to infuse capital into the Multilateral Investment Guarantee Agency (MIGA) through subscription by member countries. On the Initiatives for Heavily Indebted Poor Countries (HIPC Initiative) and for the Enhanced Structural Adjustment Facility (ESAF), my government has already agreed to contribute its entire balances in the second Special Contingency Account as a non-interest-bearing deposit toward funding these arrangements. These initiatives of multilateral institutions need to be supplemented by further measures to ensure that the transfer of resources to developing countries is maintained at an appropriate level. In particular, there is an urgent need to review the international commitment to the International Development Association.

Infrastructure development is the key to rapid economic growth in developing countries, and we are very happy that the Bank Group is charting an active role for itself in promoting private investment in infrastructure. We strongly support this initiative.

India is the largest functioning democracy in the world with all the attributes of a free society, ensuring that good governance is in place. The government of India is fully committed to deal with the menace of corruption, which is reflected in the statements of the Prime Minister of India made in various forums.

Let me take this opportunity to apprise this distinguished gathering of the recent developments in the Indian economy. We are indeed happy that our structural program of economic reforms and commitment to macroeconomic stability continue to yield substantial rewards. In 1996/97, the Indian economy grew by 6.8 percent. Growth has averaged 7 percent in the last three years. Inflation has been brought under control and is currently at an annual rate of about 4 percent. The central government's fiscal deficit declined to 5 percent of GDP in 1996/97 and is budgeted at 4.5 percent for 1997/98. The external sector has remained strong, with the current account deficit at 1 percent of GDP in 1996/97, and it is expected to be about 1.5 percent in 1997/98. The debt-service ratio is projected to decline substantially, from 25.4 percent in 1996/97 to about 21 percent in 1997/98. Foreign currency reserves (excluding gold and SDRs) increased by $5 billion in 1996/97 and by a further $4 billion in the first five months of 1997/98. These reserves stood at $25.5 billion as of mid-September. Foreign investment rose to nearly $6 billion in 1996/97 and is expected to be substantially higher in the current fiscal year, 1997/98. All in all, the economic fundamentals are strong.

We are deeply conscious that, to maintain and improve on a strong economic record, we have to deepen economic reforms and conduct vigilant economic management. Our reforms have accorded special attention to the financial sector. Our banking prudential standards have been strengthened to be comparable to the international ones. We use both on-site and off-site supervision of banks. The government securities market has been widened, with the introduction of new instruments with an array of maturities that are sold on an auction basis. Stock market reforms have been pursued vigorously. Monetary policy has been made more flexible, with virtual deregulation of interest rates and sharp reduction of reserve requirements. The exchange rate is market determined. Restrictions on the current account of balance of payments have been eliminated. We are exploring possibilities of capital account liberalization. An expert committee recently submitted a report providing a road map on capital account convertibility. This is under examination by the central bank and the government of India.

Let me not give the impression that we do not face any policy challenges. Very recently, we have had to deal with the problem of coping with a large wage settlement for government employees. In order to contain the fiscal deficit at the budgeted level, the government has acted promptly to raise fresh taxes, cut expenditure, and expand the program of disinvestment of government-owned enterprises. We have also had to tackle the problem of large capital inflows in the context of monetary and exchange rate management. Our experience shows that monetary and financial policies geared to maintain a reasonable degree of price stability can serve the purpose of not only maintaining a stable domestic environment, but also avoiding the need for disruptive exchange rate adjustment.

We are aware that we still have to tackle the problem of poverty. We are, however, confident that, with an external environment that is conducive, the Indian economy will be able to realize a sustained growth of more than 7 percent a year, which, besides enhancing living standards in general, will directly reduce poverty and provide resources for expanding programs of social development.

Statement by the Governor of the Bank for Indonesia

Mar'ie Muhammad

This annual meeting takes place in the course of currency turmoil in the Southeast Asian region. Indeed, over the last decade the Southeast Asian economies have demonstrated tremendous progress, a development that was described by the World Bank as *The East Asian Miracle*. Despite this progress, over the last two to three years Southeast Asian economies in general are marked by the following:

- high economic growth with signs of economic overheating;
- enlarged current account deficits accompanied by inflationary pressures;
- growing short-term private foreign borrowings; and
- construction of huge projects that are beyond the limits of national economic capacity.

In addressing these issues, the countries in the region have made considerable efforts through structural adjustments. As a result, there are positive indications that the currencies are in the process of arriving at a new equilibrium in the near future. As far as Indonesia is concerned, we have taken the following major steps: floating of the rupiah since the middle of August 1997, accompanied by tightening of liquidity and increasing interest rates—this tightening is gradually being loosened, and interest rates are being lowered in measured steps; to maintain the budget in balance, the government has decided to cut the development budget by 8.4 percent and to abolish subsidies; to boost exports and to contain imports in a manner consistent with GATT; and to defer a number of government projects, state-owned enterprise (SOE) projects, and private projects related to the government and SOEs that are financed by foreign commercial borrowings and export credits. It is the government's opinion that a number of private megaprojects do not reflect the national priority; therefore, they can be postponed. The postponed and reviewed projects of the government and SOEs, and the private projects related to government and SOEs, amount to approximately $35 billion. The objective of these measures is to lower the current account deficit, which is now about 3.8 percent of GDP, to a maximum of 3 percent within the next two years.

Within a month of having begun to float, the rupiah has now reached a relatively stable exchange rate in the range of Rp 2,900 to Rp 2,950 per $1, a depreciation of about 24 percent since January 1997. This relative stability is partly a result of positive reaction of the market toward the market-friendly measures taken by the government. Fortunately, this result was achieved without sacrificing our foreign exchange reserves.

Despite the budget constraints that we are facing, the government of Indonesia reaffirms its commitment to discharge all of its financial obligations fully and in a timely manner, and will continue to make efforts to prepay our foreign debt using proceeds from on-going privatization of our SOEs. Although we are in favor of market mechanism, we are concerned with the excessive volatility of many currencies, which undoubtedly creates uncertainties in the business community, and in turn could lead to an economic crisis. In this regard, I would urge the IMF to take an active role according to its mandate.

Meanwhile, we are impressed by, and we support, the recent approach of the World Bank in implementing the development concept in a very broad sense. We welcome the initiative taken by the World Bank and the IMF in addressing the foreign debt burden of the most severely indebted poor countries. As part of our commitment to the HIPC Initiative, the government of Indonesia has decided to contribute $10 million to the HIPC trust fund. Considering that about 1.3 billion people still live in poverty, we urge the Bank to put the poverty eradication program as its highest priority.

In my view, the goal of development is to create conditions that will enable each human being to attain his or her potential in all aspects of their lives, in creating a sound society that succeeds in preserving the harmony between community and individual interest and in maintaining the balance between rights and duties.

Finally, I wish to state that Indonesia will continue to maintain the sound and prudent economic policies that have been demonstrated over the past 30 years, and will continue to carry out effective structural reforms. As excessive volatility of currencies can hinder the world economy, we warmly welcome any regional or global initiatives to stabilize currencies.

Government Statement on Policies to Deal with the Impact of Rupiah Fluctuations

We would like to open the statement by inviting the Chairman and honored members of parliament to give praise and thanks to God Almighty, as only with His blessing and mercy will we have the strength to fulfill our duty to our nation.

In the state address delivered to the Indonesian parliament by the president of the Republic of Indonesia on August 16, 1997, the president set forth the reasons Indonesia had decided to allow the rupiah to float. Further, in the same address, a broad indication was given of the policy direction that would be followed by the government to deal with the impact of the floating of the rupiah that occurred after intervention band was suspended. Experience from other countries has shown that in the early stages of a floating exchange rate system, substantial fluctuations in the value of the currency will take place. This fluctuation is generally short lived and is caused largely by market players and persons who are in process of learning how to deal with the new reality. This initial condition can be exacerbated by speculations. Moreover at this early stage the currency is still in the process reaching a new equilibrium.

Even though in the early stages of a floating exchange rate system there is likely to be excessive volatility, we note that since the beginning of September the rupiah has been relatively stable with the exchange rate moving between Rp 2,900/$1 to Rp 2,950/$1. This favorable outcome reflects various government efforts that were positively received by the market.

The currency fluctuations have had a substantial effect on business activities as well as on our national development programs. The changing value of the rupiah has influenced government receipts as well as the forecast annual expenditures in the state budget for 1997/1998. Even though there is a considerable negative impact, we hope this event can be used as an opportunity to consolidate the national economy by implementing various structural adjustments. These structural adjustments are needed so that all sectors of our national economy are prepared to face economic globalization, a development that is already well under way.

The Southeast Asia currency fluctuations occurred at the same time as the U.S. dollar gained strength against most other currencies, including the Japanese yen and the European currencies.

From January 1997 through 11 September 1997, the rupiah depreciated by 23.53 percent, while the Thai baht had depreciated by 36.68 percent. The weakening of the rupiah/dollar exchange rate should be seen in light of the weakening of several currencies in Southeast Asia, as well as the Japanese yen and other European currencies against the U.S. dollar. This change in the exchange rates is important if Indonesia is to maintain its competitiveness, since, in addition to the United States, Japan and Western Europe are also important markets for Indonesian exports. One difference between what happened in Indonesia and elsewhere is that Indonesia's depreciation took place without any substantial loss of our national foreign exchange reserves.

In order to stabilize the fluctuations of the rupiah and to assist in the strengthening of the national economy as soon as possible, the government will undertake a series of policy measures with the following objectives:

- stabilize the value of the rupiah at a new equilibrium level;
- strengthen fiscal policies;
- reduce the current account deficit;
- establish a sound banking sector; and
- create a vibrant private business sector.

To reach our goals we will take steps that are in line with the new situation and with market trends. These measures will have a positive effect on the development of the capital market and are in line with Indonesia's 25-year reputation for prudent economic management.

To reach the above-mentioned goals, the government is already implementing a number of policy steps and will take further measures as follows.

As the situation permits, the government will continue to reduce interest rates on SBIs, in stages. The reduction of interest rates on SBIs will help to bring down interest rates on loans. This is important for promoting the recovery of the private business sector.

The government will loosen liquidity gradually and in accordance with the situation through fiscal and monetary instruments. This easing of liquidity will be conducted cautiously so as not to give rise to additional volatility of the rupiah.

Because government revenue from direct and indirect taxes is going to decline, an adjustment to government expenditure is needed. The reduction in receipts is due to a reduction in private business activity and to numerous losses experienced by private businesses as a result of the change in the exchange rate. The state budget is also under pressure because of the size of the fuel (BBM) subsidy, currently borne by the government, which has resulted from the decline in the value of the rupiah. The fiscal year 1997/98 budget originally planned for a net profit from oil of Rp 249.2 billion. However, if the reference price of $16.5 per barrel of oil is maintained and if the exchange rate is $1 per Rp 2,900, the size of the annual BBM subsidy rises to Rp 2.2 trillion. If necessary adjustments are not made, the state budget for the current fiscal year will suffer a deficit of Rp 9.2 trillion, and for this reason steps must be taken to overcome the potential deficit.

Therefore, a number of budget programs and projects should be rescheduled, including:

- programs/projects of various ministries and government institutions;
- official travel;
- workshops, seminars, and training;
- land acquisitions, government office constructions, and procurement of equipment; and
- other development projects under Part XVI of the state budget.

The total amount of expenditure to be rescheduled comes to Rp 3,278.9 billion. This is equivalent to 12.7 percent of the rupiah development budget or 8.4 percent of the total development budget.

Projects to be rescheduled within the ministries and government institutions consist of those projects where a significant portion of all rupiah financing is used for import, those projects that have not yet begun any physical development, or those projects that have not signed the contract. Most of these projects are within the Ministry of Public Works, the Ministry of Mining and Energy, and the Ministry of Transportation.

Although we are experiencing constraints on the state budget, the government will fulfill its foreign debt obligations thoroughly and on time. If the situation permits, it may even be possible to make prepayments on foreign debt.

Various programs and projects that are directly connected to efforts to raise social welfare and overcome poverty will not be rescheduled. These programs and projects will be carried out as planned. Included in this category are various Inpres projects, the IDT program, and projects in the field of basic health and basic education. In addition, foreign aid projects whose funding source is from the CGI will be carried out as planned.

In addition to budget projects, various state-owned enterprise projects will be postponed or reviewed, primarily those with high import content or those funded from overseas. Projects that will be postponed or reviewed include:

- government projects;
- state-owned enterprise projects;
- private projects connected to the government; and
- private projects connected to state-owned enterprises whose funding source is from foreign commercial loans that require the approval of Tim PKLN (Keppres No. 39/1991) and export credit.

Such projects are divided into three categories: those that will be continued, those that will be postponed, and those that will be reviewed. Projects to be continued are those that are already under construction. These projects will be continued according to the original schedule. Projects to be postponed are those projects that have not yet begun. Implementation of these projects can be postponed until the economy recovers and the objectives of this rescheduling have been achieved. Projects to be reviewed are those projects that require further study, and based on the results of the study these projects will be either continued, postponed, or rescheduled.

From the total number of SOE projects and private projects connected to government/SOEs that are financed with commercial credits amounting to Rp 161.78 trillion, those to be postponed amount to Rp 38.92 trillion (24.1 percent) and those to be reviewed amount to Rp 62.69 trillion (38.7 percent). Within the Ministry of Mining and Energy, of the 29 power generating plants that have been negotiated, 14 of those will be postponed (amounting to $5 billion), and 9 of those will be reviewed (amounting to $4.9 billion). Furthermore, two oil refinery projects, amounting to $800 million, will be postponed. Within the transportation sector, 29 toll road projects will be postponed, and 19 toll road projects will be reviewed. The Manggarai Terminal project and the Surabaya-Madura Bridge project will be postponed. In addition, various private megaprojects, such as Menara Jakarta and the Java-Sumatera Bridge project, are not considered to be priority projects by the government, and therefore can be postponed—so can the Indonesia-Malaysia Bridge project, which is not an urgently needed project.

From government development projects financed with export credits amounting to Rp 2.37 trillion, those to be postponed amount to Rp 237.6 billion (9.4 percent) and those to be reviewed amount to Rp 970.1 billion (38.2 percent). The desired outcome from postponing and reviewing these projects is to reduce the current account deficit, so that over the next two years the current account deficit can be kept to a maximum of 3 percent of GDP.

To stimulate non-oil exports, the government will provide facilities to exporters mainly in the form of preshipment financing. In addition, import duties on a number of raw materials and intermediate products will be reduced. To further restrain the growth of imports, the government will impose and increase sales taxes on a number of luxury consumption goods (PPn BM) that are not vital for development or for basic social needs.

Consolidation and measures to improve the soundness of the banking system will continue to be carried out. Within this framework, a study on the plan to merge state banks is being completed and will be implemented as soon as possible. It is hoped that plans for the merger and acquisition of private banks will continue. Banks that are truly insolvent and whose difficulties cannot be overcome through merger or acquisition will be liquidated, while safeguarding depositors as far as possible, mainly small depositors.

Private businesses are encouraged to engage in consolidation and not to pursue unnecessary expansion activities, especially those activities that depend on short-term foreign funding. In this connection, the government also hopes that private companies will fulfill their obligations toward foreign parties.

As it realized that dealing with currency volatility requires regional and, even global, efforts, the government welcomes every effort aimed at stabilizing the various foreign exchange rates, including those in Southeast Asia, through a process of regional and global cooperation. The government will implement these measures as quickly as possible in order to provide greater certainty for the private business community and for society in general. The government seeks the support of the honorable members of parliament in these efforts and extends its appreciation for this support. May God the Almighty bless our efforts.

Statement by the Governor of the Bank for the Islamic Republic of Iran

Hossein Namazi

I would like to start by expressing my appreciation for the opportunity to discuss topics that have made their way on to the agenda of the Bretton Woods twin institutions. I would like to touch upon some of them as follows. Before proceeding, I wish to congratulate the government and people of the People's Republic of China for the rejoining of Hong Kong to the mainland and to thank them for hosting this meeting.

Strengthening Support for Development

The divergence between the growth in private capital flows and the stagnation in official flows to developing countries that has characterized the early 1990s continued in 1996. Between 1990 and 1996, when private net capital flows to developing countries grew fivefold, official development assistance had either leveled off or slightly decreased.

The Bank and the IMF's call to strengthen support for development cooperation sends a clear and timely message regarding the decline in official development assistance (ODA) flows and the very limited access of poor countries to private flows. I therefore urge donor countries to redouble their efforts to provide adequate concessional resources to the low-income countries with either limited or no access to private capital markets. Meanwhile I also urge the developing countries to increase efforts aimed at containing budget deficits and encouraging private savings to reduce dependence on external financing.

Furthermore, the task of the World Bank, as well as of other multilateral development banks and bilateral agencies, is to provide countries with the kind of assistance they really need. Middle-income countries that have easier access to private financing need a different type of assistance than do low-income countries with fragile state institutions and less open economies. This means that the Bank should provide middle-income countries with more sustained support through IBRD loans as well as International Finance Corporation and Multilateral Investment Guarantee Agency instruments. Thus, more concessional resources could be used to increase the attractiveness of poor countries for the private sector and to reduce poverty. In this respect, I support the general approach of the Bank's Strategic Compact to make the Bank's products and services more client tailored.

Implementing the HIPC Initiative

The decline of ODA flows emphasizes the need for developing countries to become progressively less dependent on ODA. In this context, a sustainable debt policy is crucial. We therefore welcome the progress that has been made with regard to implementation of the HIPC Initiative since the last meeting and would like to commend the Bank and the Fund for their leadership in this endeavor.

Nevertheless, the experience gained thus far from four HIPC Initiative cases has revealed some practical difficulties. This reflects the complexity of the issues and calls for exercising flexibility in the application of the provisions and for a strong commitment to cover the costs on an equitable basis.

The Strategic Compact

In recognition of the rapidly changing global environment, the World Bank Group has adopted a program of renewal that will enable it to position itself well for the twenty-first century. The Bank's traditional ways of doing business are being changed to reflect the new political and economic environment influenced by increased globalization, client diversity, and the technological revolution.

We welcome this shift to a broader development agenda, especially in terms of more socially relevant country assistance strategies and better targeted projects based on a more comprehensive understanding of local social situations and better assessment of the social and political risks. We believe it is a sound approach. Nevertheless, it is essential for the Bank and the IMF to stay within their respective mandate.

However, within the topics covered by the Strategic Compact, I would like here to touch upon the issues of governance and combating corruption. Before turning to these issues, I would like to draw your attention to the importance of careful consideration of the cost-effectiveness of implementing the Strategic Compact.

Governance and Combating Corruption

Worldwide attention to issues of governance has intensified in recent years so that it has become a central item on the agenda of the international financial organizations in their dealings with member states. Promoting good governance in all its aspects, including ensuring the rule of law, improving efficiency and accountability of the public sector, and tackling corruption is identified as an essential element of a framework within which economies can prosper. Corruption in economic activity and, more specifically, bribery is one manifestation of weak governance and is a major concern of governments, citizens, and nongovernmental organizations in developing and industrial countries alike. The heightened focus of the World Bank and the IMF on these topics is particularly welcome. We find this initiative positive and believe that good governance and the move to combat corruption contribute strongly to sustainable growth, social development, and the creation of a stable regulatory environment at national and international levels.

However, certain points are noteworthy in this context: first, the principles of accountability, participation, and transparency that the international financial institutions are applying to borrowing governments have not as yet been rigorously applied to the institutions' own governance. While pressure for good governance has been magnified by the policymaking role of the Bretton Woods twins, neither institution has adequately reformed core aspects of their own accountability and participation.

The World Bank and the IMF fall short of these requirements of good governance in a number of ways, despite their efforts to respond to calls for more transparent, accountable, and participatory governance. In both institutions there are certain rules that work against the standards of governance that they are requiring from member governments.

Second, as we stated at the last Annual Meetings, despite all the constructive intentions that might have been behind the idea of requiring good governance, there is a major concern regarding its abuse—that it may serve as a tool to impinge on national sovereignty. This should be carefully dealt with by both institutions.

Third, corruption is a global phenomenon that affects all countries in varying degrees. Therefore, international cooperation among all countries should be strengthened to reduce corrupt practices. In this context the Bank's strategy for helping countries combat corruption is particularly welcome. A recent communiqué of the Development Committee indicated that the Committee had encouraged governments to criminalize international bribery. With respect to this subject, it is noteworthy that what may in one case be counted as bribery, in another case is treated as the legal payment of commissions to intermediaries. Thus, in the case of international transactions, equal attention should be paid to both sides. For example, the tax deductibility of bribes in many major exporter countries not only does not challenge corruption, but is even conducive to such practices. Therefore, a general agreement on bribery is required at the international level to ensure that the legal and constitutional definitions of corruption adopted by different governments are compatible, so that a crime committed in one jurisdiction will be recognized as such by others.

It is noteworthy that the Islamic Law, which is based on the instructions of the Holy Quran as well as the rules enacted by the Prophet Mohammed has precisely touched the bribery issues, such that a Prophetic Narration establishes that "the briber and the bribee deserve hell."

Capital Account Liberalization and SDR Allocation

We support the position taken by the Ministers of the Group of Twenty-Four regarding capital account liberalization. We expect the IMF to complete its work on the orderly liberalization of capital movements as a prelude to any amendment of the Fund's Articles of Agreement. We also welcome the agreement reached on the special one-time allocation of SDRs and the quota increase. We believe that, in order to increase the role of developing countries in the decision-making process of the Bretton Woods institutions, there is a need to modify the formula for determining quotas, and we are pleased with the assurances given in this respect.

Now I would like to present an overview of economic conditions in my country. The overall economic outlook is favorable. The government, while fulfilling its undertakings and improving the external balance of payments, has succeeded in containing inflation and has decreased its rate by over 50 percent compared with the preceding year. Nevertheless, the GDP growth rate increased by 5.2 percent in real terms during the last year.

As you may know, the new administration in the Islamic Republic of Iran has recently commenced its work. This administration, while remaining committed to the earlier economic and policy reforms pursued under the country's Second Five-Year Development Plan, will mainly embark on the following fundamental tasks aimed at attaining further economic growth, greater social justice, and sustainable development:

- applying a tighter discipline to the financial system of the public sector;
- reducing government expenditures through further privatization;
- increasing tax revenues by improving the taxation system, reforming tax laws, and introducing value-added tax;
- reducing inflation through tighter monetary policy;
- promoting private savings and preventing private sector crowding out by the government;
- establishing an exchange rate system compatible with the economic growth rate;
- promoting price stability;
- making a stronger commitment to the social sectors and human resource development; and
- introducing a more efficient economic policy coordination and implementation.

Statement by the Governor of the Bank for Iraq

Rashid Hwaish

I would like to begin my brief remarks by congratulating you on your election to chair the 1997 joint Annual Meetings of the Board of Governors of the IMF and the World Bank Group. I take this opportunity to add my voice to those of my colleagues in expressing our thanks and appreciation to Hong Kong for hosting this year's meetings, the largest international economic gathering held here since it joined the People's Republic of China.

In previous years, and at these same meetings, the Iraqi delegation has brought to our attention one of the most important purposes of the IMF, as stated in paragraph 4 of the Articles of Agreement: eliminating the restrictions that hamper world trade. Today once again, I wish to affirm that the continued economic sanctions imposed on Iraq since 1990 and the freezing of its banking assets are incompatible with the Articles of Agreement and the general philosophy of the Fund. As Iraq is a founding member and one of the nations that signed the Bretton Woods agreement in 1945, we urge the IMF to condemn the continuation of economic sanctions against Iraq, based on their incompatibility with the Fund's purposes of eliminating trade restrictions and promoting economic stability and prosperity for all the nations of the world.

The economic sanctions imposed on Iraq have greatly affected the lives of its people and hindered the country's development, as can be seen from the direct effects of sanctions on the production of goods and services in all sectors of the economy, from rising inflation and the resulting negative impact on family income, and from the severe shortages of medicines and medical supplies that have resulted in rising death rates in all age sectors, not to mention pollution of the environment and its negative effects on the quality of life in Iraq.

Despite the expiration of the first phase established by the memorandum of understanding between Iraq and the United Nations, signed in March 1997 and permitting Iraq to export limited quantities of oil, and despite the renewal of the memorandum in August 1997 for an additional six months, the situation in Iraq remains very difficult. During implementation of phase one, many difficulties were encountered in the contracting process. Three months after the expiration of phase one in June of this year, the import program for crucial items has still not been implemented, and contracts have been suspended without justification—despite the urgent need for these items—owing to the position of certain countries that have placed obstacles in the path of its implementation.

From this international forum today, we call for measures to ensure the rapid implementation of contracts to purchase food, medicine, and other basic necessities, in exchange for oil exports, in accordance with the second phase of the memorandum of understanding.

After seven long years of sanctions against my country, which are without precedent in modern history, and in view of our patience and continued efforts to implement the relevant Security Council resolutions, the international community and its representative institutions are demanding a review of our experience with the commission responsible for implementing the terms of the sanctions against Iraq and a revision of their operating methods. A new and just system must be developed that will prevent any of the commission's members from using the right of veto or creating delays and obstacles, whether for political purposes or for any other reason, to obstruct the importing of goods or the provision of services crucial to the lives of an entire people who are members of the international community.

Once again, I appeal to the IMF and the World Bank, based on the principles of their Articles of Agreement and the Declaration on Partnership for Sustainable Global Growth, approved by the IMF's Interim Committee on September 29, 1996, to call for an end to the economic sanctions imposed on Iraq and the freezing of its assets. I also appeal to the Governors of our financial institutions, Ministers of Finance, and governors of central banks, to invite your governments to work together to lift the sanctions and end the suffering of an entire population caused by the deterioration of their economic and social conditions. Implementation of the memorandum of understanding signed by the Secretary General of the United Nations has not been sufficient to halt the continuing deterioration of the quality of life in Iraq, and the continuation of sanctions will lead to an immense human tragedy, unless measures are taken to end this abnormal situation, after Iraq has fulfilled all its obligations in accordance with the relevant resolutions.

Most developing countries currently face the prospect of deteriorating production systems, caused by the threat of free markets and prohibitions against any financial or administrative restrictions on the transfer of goods to world markets and against subsidizing goods produced for export. Faced with higher costs and lower technical standards, our production installations will encounter many difficulties caused by application of the General Agreement on Tariffs and Trade agreement and membership in the World Trade Organization. That is why the IMF and the World Bank are calling for added support for developing countries' efforts to make the necessary adjustments and develop their production systems, thereby increasing their ability to penetrate world markets and meet the challenges of free trade.

Statement by the Governor of the Bank and the Fund for Ireland

Charlie McCreevy

The IMF and the World Bank have done valuable work during the past year. Ireland particularly welcomes the advances made with a number of initiatives to help the less developed countries and their integration into the world economy. Regarding the economic situation, the *World Economic Outlook* makes for encouraging reading but equally shows that policymakers face considerable challenges.

Irish Economy

The Irish economy has made impressive progress in recent years. This year is also proving very positive. GNP is likely to grow by about 6.5 percent, with employment rising by about 4 percent and unemployment declining further. Investment continues to grow strongly. Inflation should average 1.5 percent in 1997. The long-standing policy stance that has brought about these results will be maintained.

Current Issues

I would like to comment on a number of issues relevant to the Fund and the Bank on which progress has been made since our last Annual Meetings.

I am particularly pleased to note the preparatory work that has been initiated in the IMF in relation to Economic and Monetary Union (EMU) in the European Union (EU). This major change to the European region's economic and monetary systems will have implications for the global economy and also for the relationship between the Fund and the European Union and its member states. I am very pleased to see the cooperative and mutually supportive manner in which the discussions between the Fund and the EU are being handled.

In the EU, preparation for this major project has progressed in a major way—on both the policy and practical aspects—over the past 12 months. I am confident that EMU will be established on January 1, 1999, in accordance with the treaty timetable. It is clear, too, that Ireland will qualify for participation from the outset. There is every reason to believe that EMU will be characterized by a low inflation and low interest rate environment conducive to economic growth and sustainable employment creation.

We note with approval the agreement on the special one-time allocation of SDRs to bring total allocations to all members to a common benchmark of quota.

We warmly welcome the agreement to strengthen the financial base of the Fund to meet future challenges through the Eleventh General Review of Quotas. A positive aspect of the agreement is that it will bring quotas more into line with relative positions in the world economy.

We fully agree with the concept of making the orderly liberalization of capital movements one of the purposes of the Fund and with extending the Fund's jurisdiction to capital movements.

Development Agenda

Turning to the development agenda, the Bank and the Fund are to be congratulated on the progress that has been made on the implementation of the Initiative for Heavily Indebted Poor Countries (HIPC Initiative). We very much welcome that decisions have been made on Uganda, Bolivia, and Burkina Faso and that preliminary consideration of a group of other countries is well under way. This is no mean achievement, given the complexity of the problems affecting the indebted countries and the number and diversity of the players that are party to each decision.

We note the flexibility with which the initiative is being implemented. It is important that this flexibility be used to ensure that the maximum number of eligible countries benefit from the initiative—and as early as possible.

In any event, the initiative must offer a real exit from excessive debt to the countries concerned and allow them to regenerate their capacity for economic and social development. In this context, Ireland welcomes the recent internal review of the Enhanced Structural Adjustment Facility (ESAF), and looks forward to the completion of the ongoing external evaluation. Understanding the impact of structural adjustment, on social sector programs in particular, is critical to implementing the ESAF in an optimal way.

Other Issues

The new focus on good governance by the Bank and the Fund is appropriate and timely. This is necessary for the effective implementation of macroeconomic and development policies.

The volume of business now being transacted by the Multilateral Investment Guarantee Agency (MIGA) is such that an increase in its resources will be necessary if MIGA is to meet increased demand for guarantees in coming years. We welcome the conclusions of the Development Committee that the immediate funding requirement be dealt with as soon as possible and the overall question of a capital increase be sorted out by the spring meetings.

We would encourage the Bank, in implementing its action program, to reduce barriers to private sector involvement in infrastructure in developing countries. Its sectoral and global experience, strong credit rating and financial capacity, long-standing partnerships with countries, and reputation as an honest broker equip the Bank to make a special contribution in this field.

In conclusion, I would like to congratulate both organizations for their efforts during the past year. The leadership, long-term orientation, and strategic qualities shown by those in charge of both the Fund and the Bank augur well for the future.

Statement by the Governor of the Fund for Israel

Yaakov Neeman

Thank you very much for the opportunity to address this distinguished group on behalf of the State of Israel. The joint meetings of the

International Monetary Fund and the World Bank hold great significance for the world economy and for Israel as an active participant in the world economy.

It is a great privilege to hold the meetings here in Hong Kong since handover to the People's Republic of China has been effected. The Jewish people owe a great debt to China for harboring Jewish refugees during the second World War. These refugees found haven in cities like Shanghai, Tianjin, and Harbin. I am reminded of the Talmudic expression that states, "he who saves a life, it is as if he has saved the entire world." With this spirit I would like to praise both Bretton Woods institutions and their staff for their initiative with various programs to promote and assist poor countries. In particular I would like to commend their efforts to assist the incipient Palestinian economy, and thereby promote peace. We hope that these efforts will not be undermined by recurring acts of terrorism. Such acts endanger the peace process and bring devastation to the Palestinians and to their economy. We continue to seek peace and security with the Palestinians and with all other countries in the region.

Impressive Achievements

Israel's economic achievements have been quite impressive. Today the State of Israel is a highly advanced, industrialized economy. This decade is especially remarkable. During the period 1990–96, Israel achieved GDP growth of approximately 6 percent a year, based mainly on high value-added industries such as high technology. This growth rate brought Israel to about $17,000 GDP per capita in 1996.

Decline in Growth Rate

However, in mid-1996 a decline in the growth rate occurred. It is important to emphasize that this slowdown is not a recession. Moreover, the Israeli economy has the potential for an even higher growth rate than the indicators show. In order to realize this potential in the future, and to return to a growth rate of 5–6 percent a year, in June 1996, the government of Israel acted quickly to find a solution to the problems of the previous two years.

The Problems of the Economy in 1996 and the Policy

The central problem of the economy was the large deficit in the current account of the balance of payments, which, in principle, is the result of the government's budget deficit. The balance of payments deficit in 1996 was 5.6 percent of GDP. The budget deficit was 3.9 percent of GDP, compared with the 3.6 percent planned. The government acted immediately upon entering office by implementing drastic cuts in the budget for 1997. The planned budget deficit for 1997 is 2.8 percent of GDP, in accordance with the Maastricht criteria.

The government also announced a gradual reduction in the budget deficit, with a ultimate target for the year 2001—a deficit of 1.5 percent. In order to achieve this goal the government of Israel is strictly following the course of the budget. As stressed in the IMF's *1997 Annual Report* we shall adhere to the deficit target for 1997 and the following years. I can state with confidence that this year we will not deviate from the deficit reduction goals that we set for ourselves, and the 2.8 percent target will be met.

The change in the budget deficit track was immediately reflected in a substantial improvement in the balance of payments. Today, our estimates suggest a deficit of 3.6 percent of GDP, compared with 5.6 percent in 1996, an improvement of 2 percentage points!

Policy for 1998—Budget Cut

Two weeks ago the government approved the proposed budget of 1998. This budget sets a target of further reduction in the budget deficit to 2.4 percent of GDP. It includes an additional cut in government spending, without cutting expenditure on infrastructure. It also includes the setting of inflation targets designed to bring about a further reduction in the inflation rate. It is not easy to implement a restrictive policy during a time of slower economic growth. The fear of further slowdown, combined with rising unemployment, increases the pressure to abandon restrictive fiscal policy. However, we are aware that there are times when we must exercise policy restraint in the short term in order to benefit in the long term.

Structural Reforms

Let me stress that our government, which has been in office for only 15 months, has taken strong and assertive actions to improve the economy. As I mentioned, the first step was regarding the budget. However, we also believe that reforms are essential for growth. We have embarked on a series of structural reforms that are designed to remove government influence in the marketplace, promote the growth of the private sector, and enhance competition. In today's world of globalization the changes we have made are only the start. We have started deregulating many different industries and sectors of the economy. Among the structural changes that the government approved, we can find examples in telecommunications, transportation, investments, construction, and medicine. The government, in cooperation with the Bank of Israel, has also announced a plan to remove foreign exchange controls, which will make the Israeli shekel fully convertible by mid-1998.

Privatization

In the past year, the Israeli government has labored intensively to expedite the process of bank privatization. The fruits of this effort reached a climax two weeks ago with the sale of the controlling share of the largest bank, Bank Hapoalim. The proceeds of this transaction may equal 2.1 billion dollars. It should be emphasized that the sale was carried out for a price that was 25 percent above the book value and 16 percent above its valuation on the Tel Aviv stock market. This unprecedented success reflects confidence in the Israeli economy and in its future course. The process of selling and privatizing must be handled carefully and responsibly. The importance of the process is not only in selling, but also in enhancing competition and efficiency.

The proceeds generated by our successful overall privatization policy has far exceeded our projections. Our estimates for 1997 were about $1.2 billion in revenue; today we expect a revenue of $2.5 billion. Moreover, we have raised more money this year than has ever been raised through privatization.

High Technology

The world market, with its fierce competition and almost endless possibilities, is the target of most Israeli startups today. Israel has become one of the world's leaders in the high-tech field. About one-third of our export of goods is in high-tech industries, which in the past two years has grown at an annual rate of about 15 percent. It is remarkable to notice that over 3,000 start-up high-tech projects are being conducted in Israel at present.

Financial World Markets

The world is aware of the economic possibilities that the Israeli economy has to offer. Many Israeli enterprises utilize the capital markets abroad to finance their products. Besides the United States and Canada, Israel has the largest number of companies listed on NASDAQ. Most of those companies are in the high-tech field. At the same time, foreign investment in Israel continues to increase.

Conclusion

The economic forecast for the State of Israel is promising. We are making the necessary changes so the economy will prosper. I can assure you that we will keep to our plan for economic reform. We will continue to pave the way toward a future of stability and sustainable economic growth; a reduction of the budget deficit; a reduction of the rate of inflation; and prosperity.

Finally, on behalf of the State of Israel, I would like to express my gratitude and appreciation to the Managing Director of the Fund, Mr. Michael Camdessus, and the President of the World Bank, Mr. James Wolfensohn. I would also like to thank the Executive Directors, the staff, and the Joint Secretariat for these successful and fruitful meetings.

STATEMENT BY THE GOVERNOR OF THE FUND FOR ITALY

Carlo Azeglio Ciampi

The progress of integration, the spreading of economic growth to most areas of the world, the convergence of inflation to low levels, and the sustainability of existing current account positions offer all of us the opportunity to proceed in our efforts to make lasting contributions to international stability and prosperity. We should seize this opportunity.

For many in Europe, moving forward means establishing Economic and Monetary Union (EMU) after the establishment of the single market. For others, it means completing the transition to a market economy.

Economic and financial integration is already on a well-established path. We possess good institutions, regional and global, that can help us do this, but, in the final analysis, results largely depend on our policies and choices.

One year ago, Italy was faced with a hard choice. The economy was stagnating, the budget deficit—although improving—was still at about 7 percent of GDP, and the inflation rate was double the average for the European Union (EU). At the same time, the calendar and commitments for EMU did not leave any room for slippage.

The Italian government made its choice: early participation in EMU became the guiding light of our policies. The challenge was a bold one; even, according to some, reckless. But today I can say that we are close to meeting it. Optimism must be tempered with caution, but certainly Italy is now well positioned to reap the benefits of the disinflation, fiscal adjustment, and structural reform that it has endured, despite the unfavorable cyclical circumstances of 1996 and early 1997.

The markets have appreciated our determination in facing the task of fiscal consolidation: the fall of interest rates was the reward, and it has made the adjustment not too punitive for the real economy. The primary surplus in Italy is one of the highest in the world, which makes further gains in the overall budget balance easier to obtain. Confidence is returning to households and firms. We expect output in Italy to rebound this year and to continue to grow in the next: our prudent forecasts for GDP growth of 1.2 percent in 1997 and 2.0 percent in 1998 are well within reach. Our current account balance of payments position is among the strongest in Europe. The lira reentered the exchange rate mechanism (ERM) and has remained stable in it.

It is in the area of inflation that we can see the most progress. The rate of inflation, which one year ago was the second highest in the EU, is now among the lowest: much lower than 2 percent. Behind this unique improvement, there is a radical and nontransient downturn in inflationary expectations. This was made possible by converging fiscal, monetary, and income policies: the three pillars of a society that bases its progress and its cohesion on stability.

A reform of public administration has been launched. The budget process itself has been revamped. A tax reform has been approved and is being implemented. It is innovative and has made the tax system more favorable to growth and fairer.

I have mentioned the structural components of our fiscal adjustment in order to underline our commitment to the "sustainability" of our budgetary position. We are well aware that some of the corrective actions taken with the 1997 Finance Law need to be consolidated through the implementation of structural measures and through a rigorous 1998 budget.

The process of fiscal consolidation needs to take into account a problem that is common to all industrial countries, but is especially acute in Italy and Japan: the rapid aging of the population. In Italy, we are now collectively attempting to reevaluate some of the basic features of our welfare system and to adapt it to ensure its long-term balance, and to ensure that future generations can benefit from it.

We believe that Italy can contribute to the historical change about to take place in Europe. We believe that the more countries that participate in EMU, the stronger the euro will be, provided they comply with the Maastricht criteria. We believe that the single currency will go a long way toward giving back to Europe the ability to compete in the global economy, to grow, and to create jobs.

The key problem of continental Europe is unemployment. Making progress on this front requires, in addition to the resumption of sustainable growth, substantial structural improvements—in physical and nonphysical infrastructure, to help the competitiveness of the system; in deregulation, to increase competition in the markets for goods and factors of production; in taxation, to make it less skewed against using labor; and in the functioning of the labor market and the composition of public expenditure to facilitate lifelong education and training of the labor force and to increase the ability of workers to move within and across industries and regions.

Solid international institutions, regional and global, can help our societies change and prosper. We are fortunate to have the IMF and the

World Bank at work in their respective spheres, adapting to the emerging world realities while at the same time helping to shape them. The IMF is becoming a major supplier of credibility, aside from credit, to member countries and a key player in preventing and handling crises. To fulfill its complex and evolving roles, the IMF must have a clear mandate, flexibility of action, and adequate resources.

For these reasons, we have supported the establishment of the New Arrangements to Borrow, the expansion of the ordinary resources of the IMF, and the extension of its mandate to capital account convertibility. We are happy to see the first two objectives reached.

The amendment of the Articles of Agreement that we are now contemplating is an event of historical dimensions. After the successful establishment of the World Trade Organization, the extension of the IMF's responsibility from current to capital accounts would constitute a major advancement in the existing world economic order. We must therefore take care to act judiciously. In this area, it is more important to be right than to be quick.

In the same spirit, we support the emphasis that the World Bank Group is placing on the fundamental areas of private sector development and governance. The Bank can help remove existing obstacles to the participation of the private sector in the development of key areas of the economies of emerging countries by providing guarantees, supplying risk capital, extending credit, and sponsoring good sectoral policies. It can also provide critically important assistance in extending physical infrastructures and developing human capital. Governance in all countries is critical. The World Bank Group and the IMF can play a useful, if limited, role in fostering effective governance, which by its nature begins at home.

This leads me to a final consideration. In public policy, success begins at home. If we succeed there, international public action also becomes easier and more productive. To be fully effective, we must achieve mutually reinforcing results in both of these domains.

STATEMENT BY THE GOVERNOR OF THE BANK AND THE FUND FOR JAPAN

Hiroshi Mitsuzuka

Introduction

May I begin by saying what a pleasure it is for me to be able to address the Fifty-Second Annual Meetings of the World Bank Group and the International Monetary Fund.

It is extremely significant that these Annual Meetings are being held here in Hong Kong, a center of international attention, especially since its return to China on July 1, 1997. I would like to express my sincere appreciation to the government of the People's Republic of China for making it possible to hold these important Annual Meetings in Hong Kong.

May I also take this opportunity to voice my hope that Hong Kong, which has attained remarkable economic growth as a model of a free and open economy, will continue to play a significant role in the progress of the region as an international trade and world financial center, while maintaining its free and open system under the principle of "one country, two systems."

Dynamics of Emerging Economies in Asia

Let me begin by reviewing the state of the emerging economies in Asia and what lies ahead for them.

In recent years, the growth of the emerging economies in Asia has indeed been spectacular. As a growth center of the world, they have served as the engine for world economic growth. The key driving force behind such economic growth is a combination of many factors: the promotion of open-market and export-oriented policies; development of human resources; and financial liberalization, plus the enormous private capital inflows resulting from this.

However, I must point out that depending on short-term capital without having the appropriate macroeconomic policies and foreign exchange systems is dangerous. Without sound economic management, short-term capital flows can fluctuate both abruptly and on a large scale in response to changes in economic circumstances or speculative pressures, causing a currency crisis. Once a currency crisis occurs in one market, it may have an immediate and contagion effect on other markets. This will certainly have a negative impact on the sustainable growth of an entire regional economy.

The recent currency crisis in Thailand was the unfortunate realization of such concern. Happily, however, a strong relief package was arranged in a very short period of time by some Asian countries and multilateral development banks, with the IMF playing a central role in coordinating the package.

It is noteworthy that the Asian countries have expressed their willingness to provide active support, and have taken part in bringing the package together. I believe this also indicates the level of their commitment to stability in the Asian financial markets.

Lessons also must be learned from our experience in Thailand, as it has clarified a number of issues in the area of economic management that must be addressed in the wake of integration of financial markets.

First, an appropriate foreign exchange system and sound fiscal and monetary policies are both essential to currency stability. Second, appropriate policy action in response to structural problems in each country's financial sector is also essential, especially in the wake of capital liberalization. Third, close regional cooperation is essential for the prevention and control of crises, especially among the emerging economies in Asia, as turbulence in one market can easily spread to the rest of the region.

These are the challenges that we must all address, together with the Fund and the Bank. The good news is that generally the Asian countries enjoy relatively good economic fundamentals. So, if lessons are learned from the recent experience and the economy is managed properly, the emerging economies of Asia should continue to grow at a high pace in the future.

Role of the Fund and Strengthening Its Function in the Wake of Capital Liberalization

Now I will comment on the role expected of the IMF in the wake of capital liberalization.

Today, integration of the financial markets and capital liberalization are already irreversible trends. These will ensure efficient distribution of resources and have a positive effect on economic growth. In promoting capital liberalization, the Fund should play a central role as the organization that oversees the international monetary system. In this context, the proposed amendment of the Fund's Articles of Agreement to make the promotion of capital account liberalization a specific purpose of the Fund is extremely significant. It is hoped that further progress will be made in the discussion on the amendment.

In view of the recent currency crises in various parts of the world, however, the risks associated with capital account liberalization must also be taken into account in drafting the actual amendment. It is essential that the amended Articles have adequate levels of flexibility that will allow a response according to the size of the economy and the development stage of the financial market in each country.

On the other hand, we must not overlook the fact that in the wake of capital liberalization, each country more than ever is faced with the risk of being exposed to abrupt as well as large-scale capital movements. For the Fund to maintain stability in the international monetary system under such circumstances, it is essential that it strengthen its activities. To this end, a strengthening of the financial resources of the Fund is the necessary first step. For its part, the government of Japan completed on September 8 the domestic procedures needed for the New Arrangements to Borrow (NAB) and has notified the Fund of our adherence. It is hoped that other member countries will also complete their domestic procedures so that the NAB will take effect very soon.

At the same time, we welcome the agreement on the Eleventh General Review of Quotas. However, as was evidenced by the recent financial support to Thailand, the financial resources of the Fund need to be enhanced further. For future reviews of quotas, we must take into account the expected magnitude of financial crises that might result from the liberalization of capital movements.

With regard to the allocation of SDRs, I welcome the latest agreement at the Executive Board of the Fund to make the first allocation of SDRs since 1981. The agreement is most welcome because it will achieve greater equity.

Furthermore, I believe it is essential that the Fund strengthen its surveillance of the economic policy and financial markets of each member country. The Fund is also expected to provide expanded technical assistance to help develop sound financial markets through strengthened supervision of financial institutions and increased transparency of their operations. These efforts are vital as they will translate into greater discipline in financial markets and more effective prevention of crises.

Sustainable Growth of Developing Countries

I will now touch upon what is needed to ensure sustainable growth of developing countries.

First of all, it is essential that they strengthen the base for further economic growth by modernizing industrial structure and developing infrastructure. For example, Asia has an enormous need for infrastructure development. Though the public sector will continue to play a significant role in this area, there is a limit as to what and how much the public sector alone can do. This is where multilateral development banks can play a significant role by promoting private capital flows for infrastructure development.

In this respect, I welcome the action program that the World Bank Group presented at this Development Committee in response to the proposal the Governor of Japan made at the last Annual Meetings. I strongly hope that the entire World Bank Group will actively implement the action program to deliver results on the ground.

For the same reason, it is essential to strengthen and expand guarantees of the World Bank Group. In particular, with its activities steadily expanding in recent years, MIGA needs additional financial resources to continue its activities. We welcome the agreement on the adequate level of MIGA's capital increase reached at this Development Committee, and at the same time strongly urge the MIGA Board and other relevant parties to come to closure on details of the capital increase before the next Development Committee Meeting in April 1998.

Second, developing and strengthening financial and capital markets is vital for sustainable growth of developing countries. For these countries to fully benefit from globalization, it is essential that they win investor confidence and increase efficiency of their domestic financial markets by implementing financial reforms. Developing and strengthening financial and capital markets are also indispensable to steadily facilitating private infrastructure development. In the recent currency crisis in Thailand, the Bank played a key role. Thus, we strongly hope that multilateral development banks will make a comprehensive study and strengthen their activities in this field.

Third, poverty reduction and environmental protection are necessary for sustainable growth. In Asia, over 900 million people still live in poverty, accounting for about two-thirds of the world's poor; in sub-Saharan Africa, over 200 million people live in poverty. In tackling this problem, it is essential to increase employment and income through sustainable growth, while emphasizing expanded measures targeted to these populations. In view of assisting heavily indebted poor countries, Japan is ready to make its utmost contribution to the HIPC Initiative.

Many environmental issues require concerted efforts across borders. In this context, the Bank should be the forerunner among the multilateral development banks. In particular, the functions of the Global Environment Facility should be strengthened. In formulating country assistance strategies, the Bank should also strengthen policy dialogue with each country to ensure that environmental policies are strictly adhered to medium- and long-term development strategies.

For its part, the government of Japan stands ready to support such areas as promoting private capital flows, strengthening the financial sector, and fighting against poverty and environmental destruction by further utilizing the Japan Special Trust Fund in the Bank, entitled the Policy and Human Resources Development Fund, based on further discussion with the Bank.

In Japan, we are more actively addressing global environmental problems such as global warming and acid rain. Regarding antipollution and global conservation measures, our government decided to ease official development assistance (ODA) loan conditions to the level equivalent to those of the International Development Association (IDA). This policy was implemented this month prior to the Third Session of the Conference of the Parties to the United Nations Framework Convention on Climate Change to be held in Kyoto this coming December.

Finally, continual effort to maintain development assistance is equally important. The government of Japan intends to provide as much assistance as possible under the severe fiscal constraints; however, it is also necessary for the multilateral development banks (MDBs) to provide even more efficient and effective operations.

In this respect, the government of Japan supports the framework of the Strategic Compact while, at the same time, urges the Bank to attach greater importance to efficiency of its activities.

Moreover, strengthened collaboration among MDBs, other donors, the private sector, and nongovernmental organizations is an effective factor for maximizing the aid impact. I believe it is important to fully consider a wider range of opinions on development issues, including the role of MDBs, to build support for development assistance.

Conclusion

Each country's circumstances are different. Each has a different industrial structure, and is at a different stage of development: some economies are developed; some are developing; some are in transition; yet others are emerging.

Despite such diversity, there is a possibility that we all might face a crisis of the type and magnitude never before experienced as the globalization and integration of financial markets proceed. Increased uncertainty associated with capital movements might also make our policy management even more difficult than it is now. These are the challenges we will have to address in order to ensure sustainable growth of the world economy.

One obvious way to address these challenges is to further promote collaboration among member countries. This is where the World Bank and the IMF can play a central role in coordinating concerted action through global as well as regional dialogue.

In closing, I strongly hope that the Annual Meetings in Hong Kong will provide an opportunity to confirm these commitments of ours and will allow us to go a step further in our collaboration.

STATEMENT BY THE GOVERNOR OF THE BANK AND THE FUND FOR KOREA

Kyong Shik Kang

Every day, dramatic changes transform the world around us. These changes demand that we adapt and innovate to stay relevant in a rapidly changing environment.

As a major regional and global financial center, Hong Kong has been held up as an example of hybrid vigor, a successful combination of Eastern culture and Western thought. Much of Hong Kong's strength lies in its ability to make full use of these resources and reinvent itself to reflect the times.

Now, once again, a part of the People's Republic of China, I have no doubt that Hong Kong's dynamism will continue to create new opportunities not only for China, but also for the rest of the world.

Role of IMF and World Bank in the New Global Economy

Hong Kong is in many ways one example of how rapid economic integration can benefit an economy. Many globalizing countries are now beginning to benefit from freer capital flows with the aid of advanced information technologies.

I'd like to take this opportunity to commend the IMF Managing Director and President Wolfensohn for reforming the IMF and the World Bank to better address the new challenges that inevitably accompany globalization and market opening.

Indeed, the recent foreign exchange crisis in Southeast Asia clearly demonstrated how indispensable the Bretton Woods institutions are to the world economy.

The IMF Quota Increase and the Quota Distribution

It is clear we must enhance the capacity of the Bretton Woods institutions, particularly the IMF, to offer appropriate policy assistance packages while combating the tactical movements of international speculative forces. To this end, we need to consider efficient measures that can effectively increase the IMF capital base.

This added capacity would enable the IMF to more successfully manage global market mechanisms, promote economic fundamentals, and avoid unnecessary turbulence.

In this context, I welcome the recent consensus that was reached among member countries regarding the Eleventh Quota Review. However, I believe the increase does not go far enough to correct quota positions vis-à-vis member countries' economic position in the world economy. The quota distribution continues to unnecessarily limit the level of contribution of some member countries in the IMF capital increase.

I believe additional corrective measures in the future, which bring quotas more in line with the current global economic map, represent the most efficient and effective way to expand the IMF's capital base.

Given the complementary nature of the Bank's relationship with the IMF, a commensurate capital share adjustment by the Bank would go far to enhance the effectiveness of the Bretton Woods institutions.

The New Arrangements to Borrow Should Be Launched Immediately

I would also like to stress the importance of the New Arrangements to Borrow (NAB), a facility that will significantly augment the IMF's ability to cope with international financial emergencies.

I urge the member countries of the NAB to make this facility operational as soon as possible.

Korea Supports Capital Account Jurisdiction Expansion

Both economic theory and practical experience suggest that financial liberalization is essential for economic development. But our experience also teaches us that, in order to be successful, financial reforms must be implemented in an appropriate macroeconomic, financial, and institutional environment with proper timing and sequencing.

The IMF's record for guiding well-sequenced current account liberalization indicates it may also be the appropriate body to guide *orderly* capital account liberalization. Thus, I consider the initiative to expand the IMF's jurisdiction to the capital account well justified. Of course, due respect should be given to the economic differences between member economies.

The Korean Economy

Balancing growth and stability has always been an elusive proposition. Although Korea's extraordinary growth story is well known, recent cyclical and structural developments have caused some difficulties for the Korean economy.

As you know, a few large corporate insolvencies have aggravated Korea's current economic situation. The government's short-term response was decisive. While taking into account market principles, measures were implemented to improve risk management and the disposition of nonperforming assets. However, it is important to realize these insolvencies are symptomatic of the Korean economy's structural imbalances, inherited from periods of condensed growth, and demonstrate the urgent need for structural adjustment.

Accordingly, the Korean government is in the midst of structurally reforming Korea's financial system. These financial reform efforts include the expansion of business boundaries, interest rate liberalization, and support for venture capital financing. A complete overhaul of Korea's central banking and financial supervisory systems is also in the making. We expect these reform efforts to dramatically alter the landscape of the Korean financial sector in the future.

I recognize many members of the international community may still have some concerns about the current health of the Korean economy. In response, I would like to point out that Korea's economic fundamentals remain sound and current economic difficulties are manageable. Korea has begun to recover from the bottom of this cyclical downturn and macroeconomic indicators are improving; we expect over 6 percent GDP growth and less than 4.5 percent inflation. More important, current account deficits are expected to substantially moderate from 5 percent last year to about 3 percent of GDP this year.

The Democratic People's Republic of Korea's Accession to Bretton Woods

I would like to take this opportunity to address the issue of the Democratic People's Republic of Korea's accession to international financial institutions. The Democratic People's Republic of Korea's accession to the Bretton Woods institutions is a sensitive issue, especially given its policy of isolation and the political and economic questions involved. However, the Democratic People's Republic of Korea's accession would expedite its integration into the world economy and contribute significantly to the political and economic stability of East Asia. The Korean government welcomes the Democratic People's Republic of Korea's future participation in these institutions and is ready to support and assist the Democratic People's Republic of Korea in the process of meeting the prerequisites of accession.

Concluding Remarks

Increased capital and information flows promise vast opportunities for global prosperity while posing an equal number of challenges. The IMF, the World Bank, and the international community must work together to take maximum advantage of these opportunities and effectively overcome the challenges. I believe that the rapid response of the Bretton Woods institutions and the international community to the turbulence in Southeast Asia was an excellent example of this collective commitment to multilateral and bilateral cooperation. Indeed, Korea's active contribution to the IMF's package for Thailand is only one indication of our readiness to undertake the cooperative responsibilities that come with a larger economy.

STATEMENT BY THE GOVERNOR OF THE BANK FOR THE LAO PEOPLE'S DEMOCRATIC REPUBLIC

Xaysomphone Phomvihane

It is a great privilege and pleasure for me to represent the government of the Lao People's Democratic Republic at the Fifty-Second Annual Meetings of the Boards of Governors of the World Bank and the IMF.

First of all, let me join my fellow Governors in thanking the government of the People's Republic of China, particularly the authorities and the people of the Hong Kong Special Administrative Region, for the warm welcome accorded to us, and in congratulating the management and staff of the Bank and the Fund for the joint efforts put into the excellent preparation of these meetings. Let me also take this opportunity to share with the meeting that two months ago, on July 23, 1997, the Lao People's Democratic Republic was officially admitted into the Association of Southeast Asian Nations (ASEAN). This is an important event for our country and demonstrates the continuous willingness of our people to contribute to cooperation and peace in the world.

In 1996, world economic growth quickened. As for the Lao People's Democratic Republic, economic growth reached 6.8 percent in 1996, which is slightly lower than the 1995 level. Agriculture, which still accounts for more than half of GDP, managed to grow by about 3 percent in 1996, even though affected by floods. Industry expanded by 14.5 percent and the services sector by 10.7 percent, which shows the increasing role of both sectors in the economy. The 1995 floods and harsh weather conditions for agricultural activities largely caused rising inflation in early 1996. Tight financial policies were successful in bringing inflation down from 20 percent to 7 percent at the end of the year.

For 1997, our country faced various difficulties:

- Natural adversity resulted in a lower harvest, especially that of rice. This, in turn, had a negative impact on GDP.
- Garment exports to Europe slowed when the general system of preferences status for the Lao People's Democratic Republic was withdrawn in 1996.
- The financial system was unable to adapt to the rapid growth of an open-market economy.
- The Southeast Asian financial crisis affected our country.

All of these have contributed to the slower growth of the economy and caused food prices, especially those of rice, to increase in many provinces, with an impact on the overall consumer price index. Nevertheless, inflation has been maintained at the level of 10 percent. The export growth at 3.7 percent a year, compared with import growth, is slow. To contain inflation, the government has undertaken a monetary policy of restricting credits and promoting operations in the primary market through treasury bills and bills of the Bank of the Lao People's Democratic Republic.

To rectify the difficult situation that resulted from the rapid growth of an open-market economy and to ensure the sustainable development of our country, the government has undertaken several measures, such as focusing on rural development as the means to alleviate poverty and closely linking this with the preservation of forestry and land resources and the environment. In addition, to promote import substitution, the government has a program to promote the manufacturing and services sector, including the textile and garment industry. Although the prospects for increasing revenue from hydropower exports are reassuring in the medium term, the garment industry is important, as the government is aware that building a vital non-hydropower sector in the economy is essential to ensuring sustained growth and to generating employment for a fast-growing population. In addition, the government promotes the production of other commodities with the view to substituting imports and boosting exports to other countries, as well as local exports.

The government's objectives and policies for 1997–2000 will aim at creating an environment conducive to a well-functioning market economy with sound management of public resources, while promoting prudent macroeconomic policies. Priority will be given to accelerating and deepening the reforms in the financial sector, the exchange rate system, the legal framework, and the economic policymaking capacity. We recognize that without continued reform in these areas there cannot be a favorable environment for sustained economic growth. It is also evident that the decisive factor in the implementation of government policy is human capital. Therefore, effort is being put into human resources development, one of the eight priority programs.

We always regard the continued and increased support of the international community, including bilateral and multilateral donors, international financial institutions, and nongovernmental organizations, as one of the important factors contributing to the success of the country's socioeconomic development plan. In particular, during the Sixth Round Table Meeting in Geneva last June, the international community pledged to provide financial support of more than $1.2 billion to our country to support the implementation of the socioeconomic development plan till the year 2000. I take this opportunity to express to all concerned our sincere gratitude and to give assurances that we will do our utmost to use these resources efficiently and fruitfully.

As in previous years, the International Development Association contributed to the development of the Lao People's Democratic Republic's economy and in 1997 extended a loan amounting to $48 million for the Third Highway Improvement Project. We recently completed the preparation of a new ESAF-supported program jointly with the IMF. The government of the Lao People's Democratic Republic greatly appreciates the Bank's and the IMF's role in supporting the socioeconomic development of the Lao People's Democratic Republic. On behalf of the Lao People's Democratic Republic government, allow me to take this opportunity to express our sincere thanks to the World Bank and the IMF, other international financial institutions, and all friendly countries for their valuable support. We truly hope that they will continue and increase their support to our country, thus helping the Lao People's Democratic Republic to overcome its status as a least developed state in a short period of time.

We congratulate the management of the Bank for its effort in improving its organizational structure to enable the Bank to be more efficient and responsive to the needs of member countries.

Statement by the Governor of the Bank for the Socialist People's Libyan Arab Jamahiriya

Mohamed A. Bait Elmal

In the name of the delegation of the Socialist People's Libyan Arab Jamahiriya, I am pleased, Mr. Chairman, to congratulate you on the occasion of being selected to the Chairmanship of this year's Board of Governors. I wish you success in moderating these meetings and achieving good results whose effects will be felt by the various nations of the world through the commitment of member countries to coordinated economic, financial, and monetary policies that take into account the needs and conditions of those nations.

Our meetings this year coincide with the great celebrations on the occasion of the return of Hong Kong to the motherland. We applaud the hospitality, generosity, and excellent preparations for making our meetings a success, and we congratulate the Chinese people on this auspicious occasion and wish them success and prosperity.

Although world economic growth is expected to reach 4 percent in 1997 and 4.5 percent in 1998, which is among the highest annual rates since the beginning of the 1970s, thanks to the performance of the world's industrialized as well as developing countries, this has been accompanied by several adverse economic developments in Southeast Asia, an important region in the world economy, owing to the currency and financial market crisis. Part of that crisis was due to external factors beyond the control of these countries as well as to the policies of the major-currency countries. The Mexican crisis at the end of 1994 and the current events in the Southeast Asian countries represent a serious development and are a source of great concern to the developing countries. Despite the positive approach of the IMF in dealing with such crises, a major part of the solution lies in the major-currency industrial countries shouldering their responsibilities for adopting economic, financial, and monetary policies that take the conditions of other countries into account. It also requires a comprehensive supervisory role by the IMF over economic indicators in various countries of the world.

While we welcome the agreement on a one-time allocation of SDRs under the amendment to the Fund's Articles of Agreement, in light of our desire to achieve general consensus, we emphasize that this should not be at the expense of the general allocation of SDRs under the Fund's existing Agreement.

In the context of increasing the Fund's resources and enabling it to strengthen its role, we hope that the Eleventh General Quota increase will be allocated equally among member countries.

The great Socialist People's Libyan Arab Jamahiriya faces arbitrary sanctions imposed by the Security Council under its Resolutions No. 748 of 1992, and No. 883 of 1993, merely on the basis of suspicion that two Libyan citizens were involved in the so-called Lockerbie case, despite agreeing to a trial of the two suspects at the International Court of Justice by Scottish judges or in a neutral country, and despite calls by numerous regional and international organizations such as the League of Arab States, the Organization of African Unity, the Islamic Conference Organization, and many sister and friendly countries for the lifting of these sanctions. However, this has not happened because of the insistence of certain Western countries on maintaining them, which is a flagrant violation of all international resolutions, covenants, and norms.

The adverse effects of those sanctions have reached all sectors and have started to have serious results. They have also hindered development programs and plans designed to advance development programs and plans in the great Socialist People's Libyan Arab Jamahiriya.

The arbitrary sanctions imposed on the Socialist People's Libyan Arab Jamahiriya have resulted in financial losses, so far estimated at more than $23 billion. I may summarize some of the financial and economic effects as follows:

- the rising financial losses resulting from the freezing of Libyan assets owing to unilateral U.S. measures and subsequent Security Council resolutions;
- denying the great Socialist People's Libyan Arab Jamahiriya the chance of utilizing financial facilities available to it from various international and regional financial and monetary organizations to which the Socialist People's Libyan Arab Jamahiriya contributes, as a result of U.S. measures preventing our country from using the dollar in settling its international transactions, as well as Security Council resolutions;
- depriving the Socialist People's Libyan Arab Jamahiriya of numerous world investment opportunities, and of the ability to use and

manage the revenues from its existing investments because these revenues are frozen; and

- an increase in the cost of imports by nearly $600 million annually as a result of the requirement to provide full coverage of credits on the one hand, and the reluctance of exporters to accept uncovered credits on the other.

In conclusion, it should be mentioned that these direct or indirect losses resulted from measures that constitute a clear violation of the covenants of international financial institutions; the provisions of the IMF Articles of Agreement, which calls for liberation of international payments; and the provisions of the World Trade Organization Agreement, which calls for removal of all barriers curtailing the flow of goods and services among countries. Therefore, we call upon the world community to lift these unjust and unjustified sanctions imposed on Libya. From this podium, we reiterate Libya's willingness to cooperate with the United Nations and the Security Council to find a just settlement to this dispute, which has lasted too long without any convincing justification.

Statement by the Governor of the Bank for the Republic of Lithuania

Algirdas G. Semeta

On behalf of the Baltic countries—Estonia, Latvia, and Lithuania—I would like to express my gratitude to the people and governments of the People's Republic of China and Hong Kong for their hospitality during the Annual Meetings of the World Bank Group and the International Monetary Fund.

The roles of the World Bank Group and the International Monetary Fund in the global arena remain strong and important. Fundamental changes worldwide are reflected in the Bank's policy objectives as expressed in the Strategic Compact.

We welcome the World Bank's efforts to improve its responsiveness to client needs, including decentralization, by placing the country director for Poland and the Baltic countries in Warsaw. The Baltic countries support the Bank's renewal process, and we hope to see a more flexible and results-oriented Bank in the future.

Since regaining independence, the Baltic countries have achieved a stable democracy and have made considerable political and economic progress. Our economies are driven by a vibrant private sector. More than two-thirds of GDP is produced in the private sector, with GDP growth likely to remain above 5 percent for several years. Inflation is on a steadily declining trend and, in all three countries, is expected to fall to a single digit in 1997. Our inflation gains are reflected in the decline in interest rates. The rates on short-term government treasuries have fallen to less than 6 percent this year. The Baltic states remain low-debt countries, a situation unlikely to change because of tight fiscal policies in all three countries. The gross public debt and the budget deficit as a percentage of GDP are well below the limits set out by the Maastricht agreement. Structural reforms have been accelerated, particularly in the area of privatization of medium- and large-scale enterprises. Privatization of large public utilities, such as telecommunications and energy sector companies, is on the agenda. Rapid privatization, together with significant improvement of the investment climate, has boosted flows of foreign direct investment into the Baltic states. Our countries have modern, well-equipped capital markets with steadily growing trade volumes.

All three countries have received investment grade ratings, maintain an open and liberal trade regime and strict fiscal and monetary policies, and have strong and freely convertible currencies.

The progress achieved by the Baltic countries in 1996 and the results of this year clearly demonstrate stronger economic growth, continued economic restructuring, and an open foreign policy, which are expected to lead to membership in the European Union (EU). EU accession is very important for the Baltic states. We welcome that Estonia has been recommended for accession negotiations. However, we believe that Latvia and Lithuania, having made strong progress last year and this year, are also ready for negotiations. Future economic cooperation in the Baltic region would be strongly supported if the EU summit in Luxembourg in December 1997 decided to allow all three countries to start negotiations at the same time. We hope that further Bank assistance to our countries will concentrate more on activity associated with EU accession and on helping our countries meet the membership criteria.

Because the economic reforms in the Baltic countries are broadly based on private sector development, we consider the Bank's action program to facilitate private involvement in infrastructure to be a satisfactory and important agenda item. Recognizing the demand of the Baltic countries for private capital flows, we support the efforts of the World Bank Group to enhance private sector development by helping to catalyze private capital flows. In this respect, we would like to see the action programs consolidated among all Bank institutions, including the Multilateral Investment Guarantee Agency and the International Finance Corporation.

We welcome that the Bank has placed combat against corruption on the agenda. The World Bank's support of countries fighting against this sickness is extremely important. The Baltic governments also have their own action programs in this area.

We believe that strengthening governance and improving accountability and transparency are the main fields that require assistance from the Bank.

On behalf of the Governors for Estonia, Latvia, and Lithuania, I would like to express my appreciation to the Bank and the Fund for supporting our countries during the past five years and to wish these institutions success in their future work.

Statement by the Governor of the Fund for Luxembourg

Jean-Claude Juncker

As Luxembourg currently holds the presidency of the Council of the European Union, I am honored to address this meeting on behalf of the Union. I will focus my speech on three subjects: the outlook for the world economy from the European perspective, the progress in the process to European Economic and Monetary Union, and some comments on how the European Union (EU) is contributing to international financial stability.

The growth pattern of the world economy appears to be satisfactory. Noninflationary growth is being sustained by low interest rates, wage moderation, and continued efforts toward sound public finances. Although there are contrasts in economic performance across countries, the fundamentals for sustained development are generally in place. Thus, we can reasonably expect growth to continue at a satisfactory pace in the next few years.

In the developing world, the median growth rate has continued to outperform that of the industrial countries, thanks to the increasing implementation of sound macroeconomic policies accompanied by efficient structural measures. A number of Southeast Asian countries, however, have recently experienced serious financial market turbulence. These developments highlight the urgent need for containing external deficits better, reducing the reliance on short-term foreign borrowing, maintaining realistic exchange rates, and strengthening fragile banking systems. In the particular case of Africa, it is encouraging to note that the average growth performance has been rising steadily over the recent past.

Among the industrial countries, the U.S. economy is growing at a sustainable rate with inflation broadly under control and unemployment figures low. In Japan also the economic environment has improved, notably through adequate fiscal and monetary policies. And European economies are also back on a positive track, supported by an improved convergence of national economies, which is demonstrated by low inflation and interest rates.

In most European countries, however, the recovery has not been strong enough to reduce high unemployment, despite the progress made over the past 12 months. Growth has been too weak in the recent past, but above all, some European countries suffer from the fact that growth creates fewer jobs than in other countries. Given this, we are conscious that the best way to increase employment is to implement the structural reforms necessary to improve the functioning of labor, product, and financial markets. This would at the same time improve growth prospects. Progress has been made over the past year, but more needs to be done. Structural reforms will have to continue, as well as the process of budgetary consolidation, which has allowed significant reductions of short- and long-term interest rates. Such perseverance will boost consumer and business confidence and can be expected to lead to higher investment and new job opportunities.

The soundly based recovery supported by structural reforms and a positive international environment is assisting European economies in their transition to Stage 3, the final stage of European Economic and Monetary Union (EMU). The introduction of the single currency will constitute a historical event opening new avenues for growth and employment in Europe and providing large opportunities for our trading partners.

Since the last meeting of the Interim Committee, further significant progress has been made in the economic convergence of member states and the technical preparations for EMU. In the spring of 1998, European heads of state or government will decide which of the member states of the EU will belong to the first group of countries with the euro as their single currency. This decision will be based on the achievement of a high degree of sustainable convergence as measured by the convergence criteria of the Maastricht Treaty, referring to government financial positions, inflation, and interest and exchange rates. On the last three, almost all member states are performing well. As regards budgetary consolidation, considerable progress is being made. While all the member states are making efforts to meet the agreed reference value, some differences of rhythms and results remain.

The strong commitment of European governments to reducing budget deficits and the stock of public debt in relation to GDP is based not only on EMU requirements but also on their common conviction that sound public finances are a precondition for sustainable economic growth. Moreover, they are convinced that European countries will have to prepare themselves for increasing demographic pressures that call for determined action to restructure and rationalize public expenditure.

European heads of state or government, meeting last June in Amsterdam, have added further significant elements to the ongoing preparation of the technical, legal, and institutional framework of EMU. First, they endorsed a stability and growth pact, which will help to maintain budgetary discipline in EMU. Second, they decided on the principles and fundamentals of a new exchange rate mechanism, which will link participating currencies of member states outside the euro area to the euro. Third, they agreed on a resolution on growth and employment, which focuses policymaking more intensively on creating favorable conditions for higher employment, and the Treaty of Amsterdam includes a new chapter in order to strengthen the coordination of member states' policies on employment. The heads of state or government have also reached complete agreement on the two regulations that constitute the legal framework for the use of the euro.

In addition, heads of state or government agreed to improve economic coordination in Stage 3 of EMU so as to give better effect to the treaty provision that member states should regard their economic policies as matters of common concern. Regarding EMU's implications for the IMF, member states of the EU will contribute to the discussion in a constructive and pragmatic manner. On some of these issues, the EU and the IMF have already started work.

The Amsterdam summit also concluded an intergovernmental conference with the decision to adopt new amendments to the EU Treaty. The modernization of the EU is now clearly under way, although further work is needed in the institutional field. Nevertheless, the results achieved in Amsterdam allow the EU to launch a process of enlargement. These negotiations will be opened as soon as possible after December 1997 and will be one of the main challenges the EU will face over the coming years.

The European countries are already major actors at the international level, while the EU itself is progressively acquiring this status. We are conscious of the responsibility that this entails and will contribute actively to promoting international cooperation. Allow me to comment briefly on our contributions in three areas: Europe's role in providing financial assistance, in cooperating with other regional bodies, and in supporting the World Bank and the IMF.

First, we are firmly committed to supporting the Initiative for the Heavily Indebted Poor Countries (HIPC Initiative). The member states, notably in the framework of the Paris Club, and the EU institutions have indicated that they will participate in the initiative on debt relief launched by the international community after the Lyons summit. They will provide an appropriate contribution to this international commitment in favor of the poorest countries of the world. This participation of the EU, together with its member states, confirms our continuing will to help developing countries toward fast and balanced progress.

Second, the European countries are already a major part of the international monetary system. A successful EMU, underpinned by sound macroeconomic and structural policies, is likely to become a major pole of that system and to contribute to its stability. In other areas, we maintain regular contacts with the Central and Eastern European countries and the European Free Trade Association and stand ready to develop similar relations with other countries or regions. Recently, on September 19, an Asia-Europe finance ministers' meeting was held in Bangkok. It illustrates our commitment to international cooperation and our wish to contribute to a stable overall economic environment.

Of course, the World Bank and the IMF continue to occupy a key role in our approach. The member states of the EU welcome the crucial contribution of these institutions to the improvement of the international economic and financial framework. We are determined to support them in their efforts to contribute, in accordance with their respective mandates, to a sound international financial and monetary system as well as to sustainable economic development.

Hence, we welcome the agreement to broaden the IMF's mandate to include the promotion of orderly and sustainable liberalization of capital movements. Movement toward increased capital account liberalization highlights the IMF's role in maintaining order in the international monetary system and the need for sustained, sound macroeconomic and structural policies.

The size of the IMF and its liquidity position need to take into account the deep changes in the world economy as well as the mandate of the institution. We therefore welcome the recent decision on the basic features of the Eleventh General Review of Quotas.

Let me add some more words on a topic that will command our particular attention over the next few months: the improvement of the World Bank's operational performance. The member states of the EU encourage the World Bank in its endeavors to adopt better working methods, and we welcome the Strategic Compact, which aims to make the Bank more cost-effective, flexible, and responsive to client needs.

Regarding the mission of the Bank, the member states of the EU will actively contribute to finding satisfactory solutions for such issues as the need for a timely increase of the assets of the Multilateral Investment Guarantee Agency.

To conclude, I would like to stress again the resolute commitment of the EU to the stability and the efficiency of the world economy. We are convinced that EMU will be a decisive contribution to that objective and are determined to do what is necessary, in full compliance with the Maastricht Treaty, to ensure that EMU starts on schedule on January 1, 1999.