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Statement by

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STATEMENT
of Mr. Aleksei L. Kudrin
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of the Board of Governors of the International Monetary Fund
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1. The Global Economy and Financial Markets

Over the last 6 months there was a noticeable increase in the rate of global economic growth, surpassing earlier expectations in practically every region. Thus, the forecast of global GDP growth for 2004 was revised to 4.9 percent, which is almost one percentage point above the year-old estimate. We welcome the encouraging improvement in the world economic situation. At the same time, we are concerned by the fact that as before, the global economy is recovering against a backdrop of persisting imbalances and risks. As previously, the U.S. growth rates continue to play a central role in supporting global growth, while current account imbalances among the main regions not only persist but even continue to deepen. This means that there is still the risk of a significant drop in the dollar's exchange rate and a slowdown in the U.S.

Under these circumstances, there is continuing urgency in the appeals for a cooperative strategy that would include components such as a medium-term fiscal consolidation in the U.S., enhancing growth potential in the euro area and Japan through structural reforms, and more exchange rate flexibility in emerging Asia.

The increase in *world oil prices* in 2004, which was unexpected in many respects, has become a new risk to the recovering global economy. Persistence of these prices at today's level may lead to some slowing of global growth (by 0.3 percentage points in 2004-2005), and to higher inflation. As it became obvious by now, in view of capacity constraints and the limited throughput of pipelines in the main oil exporting countries, the increase in deliveries of oil to the world market is not keeping up with the vigorous growth of world oil demand. Together with ongoing political instability in a number of key exporting countries, this may lead to persistence of high oil prices at least until the end of this decade. Measures to expand the productive capacities of oil exporting countries and to restrain growth of the demand for energy resources take on special importance under these conditions.

A pick-up in inflationary pressures has been observed recently, connected in part with the increase in oil prices. Should these pressures persist, tightening of monetary policy at a faster rate than anticipated today may be needed in a number of advanced economies, which may adversely affect their housing markets and consumer demand. This could complicate the conduct of monetary policy.

The economic situation in *advanced economies* has not undergone significant changes compared to April 2004. Some slowdown in the U.S. growth in the second quarter of 2004 has added another element of uncertainty. The intensity of economic recovery in Japan looks optimistic. Some recovery in the euro area takes place against a backdrop of persisting weakness of domestic demand. The tasks of medium-term fiscal consolidation, including through reforms of pension and healthcare systems, are becoming increasingly pressing in all developed countries.

We welcome the continuing improvement of the economic situation in *developing countries and emerging market economies*. This is connected in many respects with acceleration of growth in developed countries. At the same time, we would like to make note of the gradual increase in the role of new regional "centers of growth," such as China and India in Asia, and Mexico and Brazil in Latin America.

In 2004 high economic growth was observed once again in countries of the *Commonwealth of Independent States*. This was facilitated to a significant extent by solid growth in the largest economies of the region (Russia, Ukraine, and Kazakhstan). It is necessary to mention that high growth was observed both in oil-exporting and oil-importing countries and in terms of its growth rates for 2003-2004 the CIS region was second only to China (7.8 and 8 percent as opposed to 9.1 and 9 percent respectively). The dependence of CIS countries on exports of energy resources and metals is their main element of vulnerability over the medium term. In this connection, diversification of the economy is the most important priority for many of these countries. This, in turn, requires improvement of the investment climate and development of market economy institutions through further structural reform.

Significant potential for further increase of growth in the CIS region can be found in intensification of economic cooperation through fostering trade and further integration of capital markets.

2. Making IMF Surveillance More Effective and Strengthening Crisis Prevention

Surveillance is central to the work of the Fund. The global economy and international financial markets are changing, and surveillance methods need to adapt to the new realities. We believe that, on the whole, this process moves fairly quickly. After the Asian crisis efforts were made to promulgate standards for provision of statistical data and increasing transparency and for country compliance with best practices for fiscal and monetary policies. The number of countries taking part in Reports on Observance of Standards and Codes (ROSCs) and Financial Sector Assessment Programs (FSAPs) is constantly growing. We should also commend efforts underway to develop *debt sustainability assessment (DSA)* criteria, the use of *alternative economic development scenarios* when preparing Fund programs, and application of the *balance sheet approach*.

At the same time, surveillance methods should be further improved and new approaches should be applied. For example, at the last IMFC meeting we suggested implementing *regional surveillance* at the Fund. We are pleased to see that the Executive Board has decided to undertake regular discussions of the economic situation at the regional level, thereby taking an important step toward eliminating a large gap in the Fund's surveillance instruments.

It seems that another step toward improving our understanding of international financial flows and enhancing surveillance would be to heighten the Fund's attention to the problem of *migrant workers' remittances*. The lack of reliable information in this area is contributing to large errors and omissions in countries' balances of payments, which often are automatically interpreted as capital outflows or inflows. According to preliminary assessments, the total volume of inflows into developing countries from migrant workers' remittances exceeds official development assistance. We think that work needs to be done to improve the accuracy in assessing volumes of such transfers, which could be of great importance for the conduct of monetary policy, strengthening banking supervision, and simply better understanding the balances of payments of the individual countries.

3. Enhancing International Support for Low Income Countries

We welcome the progress achieved with the HIPC initiative and support the Fund's efforts to enhance international support for the low-income countries. At the same time, given the Fund's limited resources, we consider it necessary to focus its activities in this area on addressing the critical task of supporting macroeconomic stability. We support the proposal to extend the *HIPC sunset clause* to end-2006, and also restriction of potential applicants to those countries that meet HIPC eligibility criteria as of end-2004.

This said, we do not support automatic application of *topping-up* or its use in instances where a change in the net present value of the debt is associated primarily with fluctuations in exchange rates and global interest rates. In our opinion this does not represent a fundamental change in economic circumstances and, therefore, does not correspond to the intended use of the topping-up mechanism.

We attach great significance to the establishment of a transparent and effective mechanism to support external *debt sustainability* of low-income countries over the long term. In this context, we are concerned that the proposed framework for assessing debt sustainability is yet imperfect and may encourage the quick accumulation of external debt by low-income countries to levels above the thresholds of the HIPC Initiative. We think that work in this area should be continued.