BOARDS OF GOVERNORS ● 1998 ANNUAL MEETINGS ● WASHINGTON, D.C.

INTERNATIONAL MONETARY FUND
WORLD BANK GROUP
INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL FINANCE CORPORATION
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MULTILATERAL INVESTMENT GUARANTEE AGENCY

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Press Release No. 32
October 6 - 8, 1998

Statement by the Hon. **CHRISTODOULOS CHRISTODOULOU**,
Governor of the Bank for **CYPRUS**,
at the Joint Annual Discussion

MINISTER OF FINANCE AND GOVERNOR OF THE WORLD BANK FOR CYPRUS

Mr. Christodoulos Christodoulou

It is again an honour for me to address these Annual Meetings of the Governors of the International Monetary Fund and the World Bank Group.

At this time last year in Hong Kong, most Governors said that they were encouraged by the world economic outlook, despite the financial crises affecting a number of south-east Asian countries. Even though the global economy has recorded modest economic growth and relatively low inflation over the past twelve months, many more economies have displayed weaknesses and have been afflicted by financial crises. Moreover, the real and contagious negative effects of financial crises in south-east Asia have intensified and spread and have affected many other emerging and neighbouring markets. Thus, we are far more concerned about prospects for the world economy and now worry that we may be in the midst of a sharp global economic slowdown.

What can be done by Governments, regional organizations, and international financial institutions to boost global economic growth and trade and to contain the financial pressures on the more fragile economies? Should the European Central Banks and Central Banks in other major industrial countries lower interest rates? Should developing countries partly re-introduce capital controls to insulate their economies from destabilizing capital flows? Should the IMF be provided with substantially increased financial resources so that it can play a more effective role in preventing and containing financial crises? As the discussions at the Interim and Development Committee meetings in recent days have illustrated, conflicting considerations make it difficult to give clear-cut answers to these questions. However, one thing is clear that there must not be competitive currency devaluations and a retreat towards protectionism, policies which proved to be self-defeating in the 1930's.

The ability with which the IMF and the World Bank can respond adequately and quickly to financial crises and their economic and social repercussions needs to be enhanced. Unfortunately, the prospects that the 45% increase in IMF capital under the Eleventh Quota Review will be agreed by early 1999 are still uncertain at a time when the IMF's financial resources are seriously depleted. In these circumstances, consideration must be given to making alternative arrangements to enhance IMF resources.

Although the focus of financial market participants and the media have been on the problems of the so-called emerging market countries and their implications for the global economy, we must continue to assess whether the problems of the least-developed countries are being adequately dealt with. In this vein, I note that there has been further progress in implementing the HIPC debt initiative since the 1997 meetings of the Commonwealth Finance Ministers and IMF and World Bank Governors. However, there is a need for additional actions to improve the speed, breadth and eventual effective impact of the initiative and for adequate funding so that eligible countries can achieve debt sustainability as envisaged by the HIPC initiative.

In Cyprus, the economy to date seems to have been little affected by the Asian financial crisis and its repercussions. Real GDP has been increasing at an annual rate of around 4,5% and the rate of inflation is in the 2,0% to 2,5% range. The economic fundamentals of Cyprus are relatively strong and Cyprus is meeting four of the five convergence criteria of the Maastricht Treaty.

However, the unfavourable experiences of a number of countries in liberalizing their external capital accounts and financial markets too quickly have made the Cyprus authorities cautious in freeing up our markets to harmonise our policies with those of European Union Countries. In this connection, we have welcomed the advice of the IMF staff and Executive Directors at the recent consultation discussions, that have urged a carefully-sequenced approach in liberalizing our external capital account. Successful liberalization of interest rates and the domestic and external financial markets requires also that the macroeconomic balances are in place. Accordingly, in the coming weeks a package of taxation and government expenditure-restraint measures aimed at fiscal consolidation will be considered by our House of Representatives, while a bill proposing the removal of the interest rate ceiling will also be tabled at the House.

In concluding, I would stress that Cyprus will continue to support and cooperate with the Fund and the Bank in their efforts to foster a stable economic and financial environment conducive to growth and development. Also, I would like to take this opportunity to thank the management and staff of the Fund and the Bank for the constructive advice they have rendered to Cyprus.