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Statement by the Hon. **JAMES AH KOY**,
Governor of the Bank for **FIJI**,
at the Joint Annual Discussion

STATEMENT BY THE HONORABLE JAMES AH KOY,
MINISTER FOR FINANCE, REPUBLIC OF FIJI ISLANDS
AT THE JOINT ANNUAL DISCUSSIONS

It is an honour to attend the fifty-third joint Annual Meetings of the Boards of Governors of the International Monetary Fund and the World Bank Group. May I take this opportunity to congratulate you Mr Wolfgang Ruttenstorfer on your selection as Chairman for this year's meetings. I join other Governors in welcoming the Republic of Palau to the membership of the Fund and the Bank. I also wish to congratulate the President of the United States, Mr Bill Clinton, for his excellent address, which has provided us with an appropriate backdrop to our discussions at these Annual Meetings.

When we last met in Hong Kong, the lessons from the Mexican crisis were still being consolidated and the turmoil in South East Asia was considered by many analysts, including those in the Bretton Woods Institutions, to be short-lived and its effects mainly confined to the region. However, the Asian crisis, contrary to earlier estimates, continued to deepen and its impact is now global. In recent months, the market reforms in Eastern Europe, particularly in Russia, have reached a critical phase. The Japanese economy remains in recession. A few countries in South America are showing signs of serious weaknesses. World trade is beginning to fall. In summary, the prospects for the world economy have worsened significantly over the last year and there is a real danger of a global economic crisis.

Mr Chairman, at this critical juncture of the global economy, the world desperately needs economic leadership and direction. Who can and should take up this role? We all recognise that the problems that we now face are different from those that the world faced at the post war period and at the time that the Bretton Woods Institutions were established. At the heart of these modern-day problems are the cyclical effects of large outflows of capital resulting in the contraction of domestic liquidity and immense pressures on exchange rates. The severe instabilities of international financial markets have led to sharp deterioration in real incomes, heavy loss of jobs and unbearable strains on domestic financial systems. Moreover, there has been a dismal failure to localise the impact of these turmoils and a gross underestimation of their ramifications and their intensity. While market integration and liberalisation have created opportunities for growth and development, they have also created risks that need to be understood and carefully managed.

Inevitably, the developed countries must lead the world out of this difficult period. On a country basis, the world will no doubt continues to look to the United States for support given its well-balanced economic performance without inflationary pressures and low unemployment. It is also encouraging to see the strong growth prospects in Europe.

The fundamental strength in the economies of industrial countries, particularly the United States and Europe, will provide the much-needed foundation for changing the present gloomy world economic prospects.

The continuing economic leadership of the industrial countries hinges critically on their keeping inflation in-check. While the global efforts to keep inflation low are commendable, we collectively, of course, need to persevere with policies aimed at achieving fiscal and monetary stability. These policies must continue to be primarily aimed at reducing budget deficits to allow world interest rates to come down and help resuscitate economic growth in member countries around the world. In addition, the role of the Word Trade Organisation in compliance and problem resolution is important to keep world trade at an even keel. Lastly, the developing countries must show leadership in their individual economies and continue to press on with country-specific reforms that encourage trade creation through greater competitiveness.

Under this unstable and unpredictable environment, it is crucial that the Fund and the Bank provide the strong leadership required at the multilateral level to restore confidence and stability. These modern-day problems require a new approach. We are, of course, encouraged by the momentum to find a new world financial architecture. However, in our search for the fit-outs of this new architecture, I urge the Fund and the Bank to give adequate consideration to pragmatism and sovereign ownership of reforms to help minimise, in an optimal fashion, the risks that are associated with their programs of integration and liberalisation.

The traditional roles of the Bank and the Fund are obviously under scrutiny in this new global environment and I support the call for a review of these roles particularly those aimed at strengthening the supervision and monitoring of the international financial system. I am, however, not convinced that there are fundamental flaws in the policies per se. What is more obvious to me is that we must find solutions in the implementation of these policies to adequately address, in a timely fashion, market sentiments that do not truly reflect the economic fundamentals of member countries.

Mr Chairman, while we must search for a solution and do it very quickly, one aspect is clear--we must provide the Fund and the Bank with adequate resources to enable them to effectively undertake their responsibilities under the new architecture. The need for these financial resources is urgent and immediate. Indeed, the confidence of the market place on the ability of the Fund and the Bank to adequately deal with financial crisis hinges on the availability of these resources. The Managing Director of the Fund and the President of the Bank have clearly emphasised the serious constraint that tight liquidity has on their ability to meet the challenges of an integrated global economy. We, therefore, support the increase in the Fund's quota and call on member countries, that may not have done so, to meet their obligations on the replenishment of the International Development Association resources. In this regard, Mr Chairman, I am extremely encouraged by the commitment of the President of the United States to obtain the approval of Congress to the funding of the Fund and the Bank.

The issue of capital account liberalisation plays a central focus in the discussions on the new financial architecture. Mr Chairman, it is important that we clearly rededicate our political will towards capital account liberalisation. However, in so doing, we must also keep in mind our recent experiences. While long term capital flows bring major benefits to member countries, volatile short term speculative capital flows, particularly those that are driven by the "herd" mentality, will continue to present a challenge to emerging markets. Critical questions must be resolved about the proper sequencing of reforms, the need for strong supporting institutional and regulatory policies and the relative efficiency of financial market processes. In many small developing economies, financial markets are underdeveloped and the regulatory and prudential systems are still being built. In these instances, these systems would be ill equipped to handle large and volatile capital flows.

The solution to maintaining stability is not to avoid reforms but rather to better synchronize them to the absorptive capacity of individual member countries. In my view, the best way to minimise the associated risks of capital flows in developing countries is to foster an orderly liberalisation of capital movements in line with the strength and reforms of domestic financial markets. For many developing countries like Fiji, exchange controls have served us well, although this protection has not been without costs. For us, it is a question of balance – weighing the costs of financial stability against the possibility of lower investment and growth. Under conditions that are currently prevailing in the world market place, it appears prudent that these existing controls are cautiously reviewed as the domestic financial markets grow in depth and sophistication.

I fully support the policy of transparency and accountability to help market participants make sound economic judgement rather than psychological decisions. I therefore welcome initiatives that the Bank and the Fund have taken in this regard, including the data dissemination standards and the release of Public Information Notices. But our experience has shown that, irrespective of the volume of information that are made available to the markets, we cannot avoid the "herd" mentality. Unfortunately, this is the reality of the situation but I do not think it should make us any less transparent about the need to open up our policy processes for public scrutiny.

Mr Chairman, it is obvious that the costs of the crisis have been particularly heavy on the most vulnerable members of the Bank and the Fund Most of these countries are already burdened by debt. Their poverty levels are some of the highest in the world. Many of these countries are undertaking reforms to free themselves from the vicious circle of debt and lack of growth. The current crisis means they have to double their efforts if they are to go back on to a sustainable path of recovery. I, therefore, support the sentiments expressed in support of the continuation of ESAF and urge the speedy implementation of the HPIC initiative. On this point Mr Chairman, let me reiterate our continuing call for some incentives to be granted to small developing countries like Fiji which have been prudent and responsible in fulfilling their debt obligations through proper economic and financial management

We, in small island economies, clearly appreciate that the only way to survive the pressures of globalisation and liberalisation is to be competitive. I am happy to report that Fiji is taking the necessary steps to pursue this objective. We are transforming our policies and structures to support more market based, outward-oriented and private-sector-led growth. With the assistance of the Bank and the Fund, we are developing the capital market and strengthening our regulation and supervisory skills and systems. Of course, we realise that much more needs to be done to guarantee Fiji's future in this new and fragile environment. In this difficult endeavour, Fiji will continue to look to the Fund and the Bank for assistance in developing our infrastructure, training our human capital, strengthening the capacities of our key institutions and formulating prudent and proactive economic policies.

I conclude by thanking the Bank and the Fund for their past and ongoing assistance and support for Fiji and the Region. I wish the Bank and the Fund well in their next year of operation.