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Statement by the Hon. **MATO CRKVENAC**,
Governor of the Bank for the **REPUBLIC OF CROATIA**,
at the Joint Annual Discussion

**Statement by the Hon. Mato Crkvenac,
Governor of the Bank for the Republic of Croatia,
at the Joint Annual Discussion**

Mr. Chairman, honorable delegates, ladies and gentlemen.

It is a great pleasure and privilege to address the 2000 Annual Meeting of the Boards of Governors of the Bank and the Fund here in Prague.

I would like to take this opportunity to warmly thank Mr. Wolfensohn and Mr. Köhler for their achievements and for all continuing support the Bank and the Fund have extended to Croatia and other countries. Our gratitude is also intended for former Managing Director of the Fund, Mr. Camdessus.

Allow me first to refer briefly to economic developments and achievements in the Republic of Croatia. After Parliamentary elections held in January 2000, our new government inherited Croatia in recession and facing a number of structural issues. The growth of fiscal expenditure, which has been going on continuously for years, has forced the central bank to operate a tight monetary policy. The banking consolidation seems to have finally reached its last stage. Steps that had to be taken in this regard have left their traces: namely, financial obligations that unfortunately arose from the restructuring to enhance the soundness of financial sector, but also from the repayment of arrears and commitments related to the social sector and major infrastructure project that had to be duly serviced.

The program of the current government of the Republic of Croatia is one of substantial political change. It is based on a fundamental commitment to the building of a democratic civil society with an open market-oriented economy integrated into the European and global economy. The Croatian government has decisively begun to achieve balanced public finances, with more efficient budget management, reduced public spending, and intensified structural changes aimed at fostering faster growth and development. In 2000, the first year of the implementation of this government's program, it is our obligation to strengthen the economic recovery and to create foundations for sound and sustainable economic and social development over the coming years as the program is fully implemented.

The government's overall economic program and policy measures are supportive of further economic stability, with stable prices and low inflation, a stable rate of exchange with concurrent economic growth, a faster rate of employment, and higher output and exports. Recent economic developments show a significant shift in economic trends. After -0.3% growth in 1999, economy grew at an annual rate of 4.0% in the first six months of 2000 and industrial production rose 3.0% on a year-on-year basis to June 2000. The central government budget was decreased in nominal terms by 1.2%, state official salaries were decreased by 30%, and all public sector wages by 5%. The government already settled 5.6

billion kuna in arrears out of a total of 9.5 billion kuna that were unsettled at the beginning of 2000. Tourism is expected to rise 30% compared to 1999. The current account deficit has been improved by 5% in the first five months of 2000. Foreign exchange reserves reached US\$3.5 billion in August 2000 growing from US\$2.8 billion at the beginning of February. Export performance improved by 10% in the first 6 months of this year, and it is our belief that our export performance cannot be buttressed by superficial measures, such as the exchange rate changes; rather, the ability of exports to compete has to be enhanced. That, in turn, can only be achieved by increasing foreign direct investment and by improved access to markets through the WTO and full integration of Croatia into the various levels of regional organization. Accelerated privatization will see FDI inflows rise in the shorter term, while stable, credible economic policies and a more efficient legal system will provide a basis for increased greenfield investments.

Through its program and actions undertaken so far, the new government has proved its readiness for development and the intensifying of constructive cooperation and Croatia's relationship with the European Union and international financial and other institutions., The government especially stresses the importance of the timely introduction of systematic reforms in order to democratize all institutions, strengthen compliance with human rights and basic freedoms, implement more intensive economic reforms, reconcile ethnic differences, develop peace in the region, and achieve overall cooperation and stability.

With accession to the WTO, Croatia will meet one of the two most important conditions for joining CEFTA, which, together with the Association Agreement with the EU, is one of the main preconditions and necessary requirements for increased investor interest. We are pleased with the Partnership for Peace membership, whereas entry into NATO remains a strategic goal of Croatia. In order to achieve an active and creative position in the Stability Pact, Croatia will continue to give high attention to activity within all three Pact tables. Croatia is prepared to assume its share of responsibility for the success of the Pact, bearing in mind the common goal—lasting peace, progress, and stability in southeast Europe.

How do we see future developments? Croatian industry and tourism are picking up, and also export industries are becoming a driving force of economic growth. Still we are well aware of the challenges facing the Croatian economy. There is much yet to be done in the restructuring sectors, from shipbuilding to agricultural and processing plants, privatization of the large public sector, and implementation of systemic measures against crime and corruption. The Croatian economy is small, and future development is possible through the adjustments of an open and export-oriented policy.

There is a need to expand and to not limit the flow of resources from the Bank. The Bank has the headroom necessary for new lending. There is a case for increasing the flow of traditional lending activities from the Bank to support critical areas, including especially infrastructure. Private sector and commercial banks have to take a larger share as well. This is an area in which we are trying to increase both public and private investment. I believe the Bank can help support this effort through a combination of direct lending and play a catalytic role in using its other instruments to facilitate new investments.

We are fully aware that the long-lasting benefits of such support cannot be expected without appropriate structural adjustments and sound macroeconomic policy. In fostering stability and sustainability of monetary, fiscal, and exchange rate policy, the support of the Fund is therefore of great importance. The Fund's expertise in these areas, as well as its relevant experience, has proved to be, in our case, an indispensable and highly beneficial part of the efforts to develop an adequate macroeconomic framework. We truly hope the successful and rewarding cooperation in these areas of core competencies of the Fund will be continued in the future as well.

Recent Fund efforts to strengthen the effectiveness of its facilities will undoubtedly encourage a more efficient use of its resources. However, these efforts should not be separated from those aimed at encouraging the sense of "ownership" as a sine qua non for successful implementation of every program.

Furthermore, let me assure you that, on our part, we shall continue to back all our activities with due transparency, which will hopefully contribute to the accountability and credibility of our macroeconomic policy.

Also to be noted are Croatia's efforts to enhance effective financial surveillance, as well as the accountability and credibility of its macroeconomics policies. In this regard, I must stress how greatly Croatia has benefited from the Fund's technical assistance and close dialogue with Fund staff this year.

Mr. Chairman, dear guests, as I have said, Croatia will keep its course toward integration into the European and Euro-Atlantic political, economic, and security structures. We consider the Fund's and the Bank's support in these matters to be of great importance. The Bank's portfolio of projects in Croatia is broad and satisfactory, and I am deeply convinced that jointly agreed operational priorities will further strengthen the Bank's engagement in Croatia and strongly contribute to a successful completion of the transition process. Croatia strongly looks forward to concluding a new arrangement with the Fund hopefully within this year.

Allow me to assure you that we look forward to future close, mutually beneficial cooperation and to express our thanks to the management and the entire staff of the Fund and the Bank for their valuable assistance and unselfishly shared expertise and knowledge. I also thank the Czech Republic and Czech authorities for their kind hospitality, which is greatly appreciated.

Let me conclude by wishing the Fund and the Bank well in their future endeavours.

Thank you very much for your kind attention.