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**Statement to the Plenary by Mr. Didier Reynders,
Governor of the Bank for Belgium**

This year the economic and financial climate has been particularly fraught with uncertainties which have in turn slowed economic growth. It is therefore incumbent on policy makers and the Bretton Woods institutions to pursue a policy that will reduce these uncertainties, establish the foundation for balanced growth, and generate hope for sustainable development throughout the world.

Economic prospects

Economic prospects have deteriorated over the past year. The reasons for the deterioration have been amply debated in this forum and need not be enumerated again. As policy makers, we must now determine what policies are needed to reverse this trend in the world economic outlook. The specific content of these policies will naturally vary from one economic zone to another, and from one country to another, reflecting the weaknesses of our individual economies. These diverse responses aside, however, we are all confronted with the same situation, namely a lack of confidence within both enterprises and households.

Domestic demand has declined, thereby slowing the growth rates of our economies, which in many industrialized countries still depend too heavily on net exports. Our task is therefore to determine the best ways to restore confidence. In so doing, we recognize that because some of the solutions are more geopolitical in nature, we can influence them only indirectly, whereas others are specifically economic and financial and are therefore our direct responsibility.

Belgium, by virtue of the fact that it is in the Euro zone, is very closely integrated with European market as a whole. The challenge of restoring confidence that Belgium faces is virtually the same challenge confronting the European Union, and the Euro zone in particular.

As steps are undertaken to restore confidence, it is essential to underscore the importance of continuing with structural reforms and of adhering to the Stability and Growth Pact, especially since significant progress has already been achieved in these areas.

Experience has proved us capable of managing adjustment in a pragmatic and realistic manner, without deviating from our medium-term objectives. However, it is important not to keep on deferring these objectives, allowing them to become "moving targets." The European Union has thus made it a practice to establish timetables and deadlines enabling it to take stock periodically and make gradual progress. This has been the approach applied to the Stability and Growth Pact and the Financial Services Action Plan, as well as to tax harmonization issues.

Failure to proceed in this manner will generate yet additional uncertainty, thereby facilitating behavior among economic agents that could jeopardize sustainable economic growth. The consequent further loss of confidence would then prompt additional precautionary saving by households in the face of perceived negative job and pension prospects. Businesses would react by deferring growth-oriented investment decisions and, undoubtedly, by increasingly refocusing on capital deepening investments. As policy makers, we must endeavor to prevent such behavior from occurring.

Risk and uncertainty nevertheless remain a threat to a global recovery, particularly where financial markets are concerned. This summer's sharp stock market decline will unquestionably have an impact on growth. The wealth effect and a decline in confidence will have a negative impact on private consumption. Venture capital for business financing will be harder to come by. The impact on the behavior of financial institutions will undoubtedly be even more troubling, given both their increased wariness concerning the quality of their debtors and their severe portfolio losses, which have made them weaker. Efforts to shore up confidence in financial stability are therefore imperative.

International financial stability

As underscored in the Monterrey Consensus, a healthy financial sector is essential for growth and development. Flexible and well-regulated financial systems are indispensable for macroeconomic and financial stability, especially in an environment characterized by increasing capital flows. The authorities of each country must ensure the health and stability of their financial sectors by adopting and implementing appropriate rules, standards, and codes. Multilateral financial institutions, for their part, have an important role to play in strengthening the financial system, by promoting sound policies and supporting their implementation.

The events of the past 12 months have shown that progress has been achieved. For example, the global financial system has withstood a number of shocks, most notably the impact from the September 11 attacks and crises affecting a number of emerging countries, and significant corrections to financial markets have been registered.

However, there is no room for complacency. The recent accounting scandals and deceptive corporate reporting that have attracted wide media attention underscore the need for the authorities to remain vigilant, continually assess the effectiveness of existing rules, and adapt them where necessary. Additional steps must also be taken to improve governance, accounting and reporting practices, and transparency within companies in order to strengthen the functioning of financial markets.

Other developments, though less obvious, still require at least as much attention. These include increasing linkages among financial markets, the consolidation of payment and settlement systems, the blurring of the borders of financial market segments, and the emergence of increasingly more complex financial institutions.

The debate on strengthening the international financial architecture has accelerated considerably recently. It is essential to maintain this momentum and continue to make progress with respect to implementation, which is often difficult and is viewed as moving too slowly.

With regard to crisis prevention, countries experiencing payment difficulties should be identified quickly, the scope of their problems should be quantified, and countries should be encouraged to take corrective measures sufficiently early. The Fund and the Bank have a key role to play in this area. A number of initiatives have already proved successful and will be pursued resolutely in the years ahead. They include strengthening oversight of the financial sector, awareness of vulnerability to crises, increased transparency on the part of the Fund and its members, compliance with standards and codes, and multilateral surveillance of capital markets.

The Bretton Woods institutions have an important role to play in helping member countries improve the health and soundness of their financial systems. The Financial Sector Assessment Program is a key component of this effort. As a sign of the importance Belgium attaches to the Program, we have invited it to evaluate our financial system.

In order to confront the challenges described earlier, Belgium has begun to restructure its procedures for financial sector regulation and supervision and has, in particular, strengthened cooperation among the authorities responsible for macro and micro prudential supervision. These new structures will soon be operational.

Financial stability cannot be assured without waging a constant and unrelenting fight against such abuses as money laundering and the financing of terrorism. I therefore unreservedly endorse the efforts of the Bretton Woods institutions and the Financial Action Task Force on Money Laundering (FATF) to collaborate in this fight and to finalize a comprehensive methodology for combating money laundering and the financing of terrorism. I also endorse the development of a specific Report on Standards and Codes incorporating all aspects of the 40 + 8 FATF recommendations. I urge all countries and territories that have not yet taken all necessary measures to implement these recommendations as soon as possible. I reaffirm Belgium's commitment to the international community's fight against the financing of terrorism

Resolution of financial crises

I have already addressed the question of crisis prevention efforts. Such efforts help to diminish the likelihood of such crises, but there is some question as to whether they can always be prevented. Accordingly, a parallel effort has been undertaken to develop ways to strengthen the ability of countries to manage financial crises properly.

At its meeting in Prague in September 2000, the IMFC adopted a framework for crisis resolution. While some progress has already been reported, there is still a need to enhance the work being done within this framework. More particularly, the involvement of the private sector in the resolution of financial crises, which is becoming increasingly recognized as a key element in international financial architecture, needs to be strengthened.

To improve the crisis resolution mechanisms, it is important to devise a more orderly and transparent arrangement for sovereign debt restructuring. Studies are currently under way for the simultaneous adoption of two parallel approaches: the “contractual” approach and the “statutory” approach.

Belgium has given these studies its full support, and believes that the two approaches are not only mutually complementary but also mutually reinforcing and inextricably intertwined. We also support the ongoing efforts to identify and clarify the modalities and rules concerning the suspension of payments and to implement the IMF’s strengthened debt strategy for countries experiencing payment arrears.

Another concept that is gaining more and more ground is that the introduction of collective action clauses (CACs) in sovereign bond contracts will guarantee, on the one hand, that all debt restructuring takes place in as orderly a manner as possible, and, on the other hand, that a minority of lenders will no longer be able to take actions capable of preventing the majority of lenders from preserving the value of their assets.

A G10 working group (the Quarles group) has studied the legal procedures underlying this contractual approach.

The objective of this group is to propose specific clauses: however, one of the key components is to urge debtors and lenders alike to effectively adopt those clauses. In conformity with the European Union’s recent political commitment to set an example in this matter, Belgium has announced its willingness to include majority action clauses and collective representation clauses in all its sovereign bonds issued under foreign legislation. While this can help bond markets and lawyers to become familiar with the clauses, there is nevertheless a risk that the CACs will not be used by the emerging countries, since they are still very concerned by the rising costs of borrowing and by the reduction of access to the financial markets that such clauses could entail.

It is therefore essential, if this G10 initiative is to be successful, to involve not only the private sector but also the emerging countries. Also, in my capacity as G10 chairman, I had the honor of opening this dialogue, as recently as this past Friday, with a certain number of emerging countries. It will be important during the next few months to deepen this dialogue and expand it to include other emerging countries.

The statutory approach to the mechanism for restructuring sovereign debt is currently in process of preparation, and due attention is being paid to the comments and reactions of the various parties involved. While the issues are very complex, substantial progress has already been made in developing the features of this ambitious approach.

The objective of this arrangement is to urge both debtors and lenders to reach timely agreement on the relieving of unsustainable debt, without having to actually have recourse to the mechanism itself. By providing the IMF with a reasonable and orderly restructuring alternative, while offering debtors real financial relief (by granting preferential status for the obtaining of new funds, and thanks to a lending policy to clear payment arrears), this mechanism could strengthen the *ex ante* credibility of the limits on access to IMF financing.

To successfully encourage lenders and debtors to conduct timely negotiations and to enable them to negotiate efficiently, the statutory arrangement must naturally work hand in hand with inclusion of the collection action clauses in the bond contracts. These clauses should create the appropriate legal framework for conducting such negotiations and for guaranteeing their success without the need to resort to the statutory mechanism.

While acknowledging the length of time and the difficulties involved in such a project, Belgium believes that the setting up of a debt restructuring mechanism is an essential component of any policy to involve the private sector in financial crisis management.

Poverty reduction

Implementation of the Poverty Reduction Strategies and the HIPC Initiative has made it clear to us that the Bank and the Fund, together with the other donors, both multilateral and bilateral, have an essential role to play in helping the poorest countries regain their footing on the path to sustainable development. This strengthened partnership was also emphasized at both the Monterrey and Johannesburg conferences. It seems clear that a reduction in inequalities and a sharing of growth are the true guarantees of stability and security for all. The precise objectives of development were established in the Millennium Declaration, and the means for achieving them were also identified.

I would remind you in particular that, for its part, Belgium is committed to achieving by 2010 the objective of increasing its public development assistance to 0.7 percent of its gross national product.

There is still a need to develop targeted policies whose impact on poverty reduction and on the promotion of sustainable growth can be clearly measured and assessed. In this area, I am convinced that the Bretton Woods institutions have an important role to play.

Specifically, by collaborating with countries as they prepare their national development strategy, the World Bank and the IMF can henceforth contribute toward the implementation of policies that are effective and unequivocally oriented toward results beneficial to all. Within this framework, it is important to identify cohesive and realistic objectives, intermediate indicators capable of measuring the progress being made toward the achievement of those objectives, and institutional capacities with the ability to monitor that progress. However, to avoid development of the perception that the management of poverty reduction strategies is less the province of the beneficiary countries than of the donors, I believe it is a good idea for the governments of those countries to consider opting for alternative policies. It is also important to be careful not to adopt too ambitious an agenda, which could threaten a given country's ownership of its development process.

So why don't we start by limiting the review of results to those areas whose development offers the greatest potential in terms of poverty reduction and stimulation of economic growth, as well as to other areas where efforts have already been made with a view to collecting sufficient data to facilitate adequate oversight? Health, education and promotion of the private sector seem to respond to this double requirement.

In order that growth may be shared by all, it is also important to intensify efforts in the direction of the most fragile populations, in particular those of countries that have only recently seen an end to a conflict situation. In this area, Belgium has been a constant driving force in the new dynamic that now seems to be evident in Central Africa, a dynamic that has led to renewed involvement by the Bretton Woods institutions in the region.

The Enhanced HIPC Initiative offers certain of the poorest countries the opportunity to lighten their unsustainable debt burden. It has become more and more evident that from now on the challenge will be to ensure that these countries remain permanently sheltered from all unsustainable external debt.

Because of growth projections that are far too optimistic and harmful external shocks, several of those countries are experiencing very real difficulties in exiting permanently from their debt situation. Should the HIPC Initiative be made more flexible, or even modified as to its substance? I am convinced that the response may be viewed from three different perspectives. First of all, countries should give priority to strengthening their systems of public management to ensure that the funds released by debt relief operation are effectively used to reduce poverty. Second, the international institutions are also responsible for considering the debt sustainability issue on the basis of realistic growth and export projections. Third, lenders who have not yet proceeded to forgive debt under the HIPC Initiative should be encouraged to do so without delay. But debt remission should not be the only means by which the multilateral and bilateral donors provide support for structural reform. An additional contribution of aid in the form of concessional lending or grants should also be considered as an essential component of the strategy.