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Statement by the Hon. **DOMENICO SINISCALCO**,
Governor of the Fund for **ITALY**,
at the Joint Annual Discussion

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The Global outlook

The Annual Meetings of the IMF and the World Bank are taking place this year in a context of unprecedented global economic growth. The world is not only growing at a rapid pace but the recovery is broadly based.

Some areas and countries, like China and India, which have successfully joined the process of trade globalisation are continuing to expand at considerable rates. Sub-Saharan Africa, the poorest region in the world, is expected to grow by 4.7 percentage points in 2004, and by 5.6 over the next year.

In the industrialised world, Europe is the only region experiencing difficulties in taking full advantage of the international recovery. Persistent structural rigidities and delays in implementing the Lisbon reform agenda are hindering potential growth.

The growth momentum would benefit from progress in the WTO negotiations that have recently been given a fresh impetus.

Despite the favourable outlook, global imbalances are showing little sign of adjustment as markets continue to finance such imbalances. Oil prices remain high and extremely volatile due to persistent oil market exposure to shocks. In addition to these global risks, several emerging market economies remain vulnerable to further interest rate increases given the still very high level of debt and the persistence of currency and maturity mismatches.

Crisis prevention and surveillance

Even in a favourable environment, the Fund continues to play an essential role in identifying and monitoring vulnerabilities. Surveillance is a crucial element in the Fund's work on crisis prevention. Significant progress has been achieved over recent years, but more still needs to be done.

We urge the full implementation of the framework for assessing debt sustainability. Debt Sustainability Analysis (DSA) must become a common feature of all Article IV consultations. The Fund should undertake DSA independently of lending decisions. This may require organizational changes in the Fund's departments.

Analyzing exchange rate regimes remains a central task for Fund surveillance. A better identification of the linkages between the exchange rate and the country's policy requirements would strengthen the Fund's advice on exchange rate issues.

We welcome the growing emphasis on the regional aspects of surveillance, in order to take into account the global impact of the economic conditions and policies of the systemically important Fund members.

The Fund should continue to work to improve the framework for crisis management and resolution. The procedures for exceptional access should be fully implemented. These procedures will help prevent debtor countries and market participants from placing excessive reliance on the financial support provided by the IMF.

For countries benefiting from IMF financial assistance, the definition of sound exit strategies from IMF programs is essential to avoid the prolonged use of the Fund's resources. This includes better program design, macroeconomic and structural conditions to achieve debt sustainability, more effective conditionality and a careful consideration of the timing to regain market access.

The role of the Fund in low income countries

The Fund has a key role in helping Low Income Countries achieve the Millennium Development Goals, by providing policy advice, technical assistance and temporary balance of payments concessional support.

Surveillance needs to be tailored more effectively to the specifics of low-income countries, by looking into how a country's policies relate in the broader context of the MDGs and which corrective actions—if any—should be taken in that setting.

The new framework for debt sustainability in low income countries, which takes into account the degree of institutional strength, should provide additional information on the capabilities of countries to carry on additional debt while ensuring that additional resources are not allowed to endanger medium term sustainability. It should therefore guide a country's authorities in defining policies, and inform the decisions of multilateral and bilateral donors.

Bank-Fund collaboration in this area is necessary. Debt sustainability assessment for Low-Income countries should be the result of a collaborative effort between the two Bretton Woods Institutions. Without this, there is a risk of sending out confusing signals to the international community on the macroeconomic viability of a member country.

In the next few months important decisions should be taken concerning the future of the Poverty Reduction and Growth Facility (PRGF). After 2005, the resources available for the PRGF might prove inadequate to satisfy the expected demand without bilateral additional financing. The Fund should explore the option of an additional bilateral contribution from member countries in order to preserve its concessional lending capacity while allowing for more selectivity in PRGF loans.

At the same time, we must work together to help countries that are moving from concessional financial assistance to a surveillance–based relationship with the Fund; low access PRGF and precautionary PRGF may serve this purpose. However, more work is needed to design a precautionary PRGF and to assess the potential demand for this new instrument.

We support Policy Monitoring Arrangements (PMA) as a means of addressing the demand of countries which are pursuing sound policies and can benefit from stronger IMF signals to markets or donors, while not requiring Fund financing. PMA should have the same standards as a borrowing program and entail the same level of conditionality and involvement of the IMF Board.

The Fund needs to be engaged in a constant dialogue with other development partners. In this respect, it could leverage upon its catalytic function and help mobilize additional aid flows for low-income countries.

We welcome progress with the HIPC Initiative. Since last September six more countries have reached completion point, bringing the total to 14 countries. So far, the Initiative has been able to provide substantial debt relief to countries that have reached the decision or completion points. While debt servicing continues to decline, social expenditure is growing and now accounts for almost one half of government revenues. Thanks to the recent extension of the sunset clause, the remaining countries will also be able to join the Initiative.

However, the recent deteriorating trend in the debt dynamics of many post-completion point countries is worrying. Vulnerabilities in these countries' debt structure should be closely monitored, also by using the new framework for debt sustainability in low-income countries.

Debt relief should be granted on the basis of a country-specific debt sustainability analysis. Any deviation from this principle is likely to signify a failure of the HIPC Initiative itself. Indeed, any proposal to cancel 100 per cent debt of all the HIPCs, would imply a relaxation of the HIPC criteria which, as we all know, are intended to prevent avoid the risks of creating disincentives and morally hazardous behavior.

We call on all the remaining creditors that have still not done so to join the Initiative and provide debt relief under the agreed terms. More can be done to ensure that all creditors are on board. The IMF and the World Bank can play a more active role in persuading all creditors to participate in this Initiative.

More resources are needed to achieve the MDGs. Since the Monterrey Conference some progress has been made. The EU countries are on the right track to fully deliver on their commitment to achieve 0.39 percent of GNI by 2006. We remain committed to defining national mechanisms and instruments, also in collaboration with the private sector, to raise additional resources for development.

However, aid effectiveness requires strong absorptive capacity in receiving countries. The effective deployment of resources toward the MDGs, therefore, requires mapping specific absorptive capacity constraints against the identification of MDG-related priority areas. This analysis should take place on a country-by-country basis in the context of the existing processes. The Fund should play a greater role in the context of Art. IV consultations in addressing the constraints that undermine a timely and efficient use of additional resources.

We welcome the technical work of the Fund and the Bank on some options for financing the MDG agenda, such as the IFF and global taxation. At present, Italy is not in a position to adhere to the Facility because of its legislative, accounting and budgetary rules and procedures. Nevertheless, we can support the setting up of the IFF on a voluntary basis. In our view, additional analysis for other preferences is needed, such as the use of incentives to attract remittances to development-oriented programs or mechanisms to involve the private sector in voluntary aid schemes.

Low income countries should have appropriate voice in the Fund and in the Bank. With respect to representation, we are open to consider efforts to align the voting power of member countries more closely with their current economic status, and to explore the feasibility of other measures, provided a broad consensus could be reached. A more effective voice is first of all assured by effective participation of LIC to Board activities and deliberation. Recent decisions to strengthen such capacity go in the right direction. And further initiatives should be pursued.