

BOARDS OF GOVERNORS • 1997 ANNUAL MEETINGS • HONG KONG, CHINA

WORLD BANK GROUP

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

INTERNATIONAL FINANCE CORPORATION

INTERNATIONAL DEVELOPMENT ASSOCIATION

INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES

MULTILATERAL INVESTMENT GUARANTEE AGENCY

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INTERNATIONAL MONETARY FUND

Press Release No. 32

September 23 - 25, 1997

Statement by the Hon. **HIROSHI MITSUZUKA**,
Governor of the Bank and the Fund for **JAPAN**,
at the Joint Annual Discussion

**The Hon. Hiroshi Mitsuzuka
Minister of Finance of Japan**

Introduction

Mr. Chairman, fellow Governors, distinguished guests, ladies and gentlemen:

May I begin by saying what a pleasure it is for me to be able to address the 52nd Annual Meetings of the World Bank Group and the International Monetary Fund.

It is extremely significant that these Annual Meetings are being held here in Hong Kong, a center of international attention, especially since its return to China on July 1. I would like to express my sincere appreciation to the Government of China for making it possible to hold these important Annual Meetings in Hong Kong.

May I also take this opportunity to voice my hope that Hong Kong, which has attained remarkable economic growth as a model of a free and open economy, will continue to play a significant role in the progress of the region as an international trade and world financial center, while maintaining its free and open system under the principle of “One Country, Two Systems.”

Dynamics of Emerging Economies in Asia

Let me begin by reviewing the state of the emerging economies in Asia and what lies ahead for them.

In recent years, the growth of the emerging economies in Asia has indeed been spectacular. As a growth center of the world, they have served as the engine for world economic growth. The key driving force behind such economic growth is a combination of many factors: the promotion of open-market and export-oriented policies; development of human resources; and financial liberalization, plus the enormous private capital inflows resulting from this.

However, I must point out that depending on short-term capital without having the appropriate macroeconomic policies and foreign exchange systems is dangerous. Without sound economic management, short-term capital flows can fluctuate both abruptly and on a large scale in response to changes in economic circumstances or speculative pressures, causing a currency crisis. Once a currency crisis occurs in one market it may have an immediate and contagion effect on other markets. This will certainly have a negative impact on the sustainable growth of an entire regional economy.

The recent currency crisis in Thailand was the unfortunate realization of such concern. Happily, however, a strong relief package was arranged in a very short period of time by some Asian countries and multilateral development banks, with the IMF playing a central role in coordinating the package.

It is noteworthy that the Asian countries have expressed their willingness to provide active support, and have taken part in bringing the package together. I believe this also indicates the level of their commitment to stability in the Asian financial markets.

Lessons also must be learned from our experience in Thailand, as it has clarified a number of issues in the area of economic management that must be addressed in the wake of integration of financial markets.

First, an appropriate foreign exchange system and sound fiscal and monetary policies are both essential to currency stability.

Second, appropriate policy action in response to structural problems in each country's financial sector is also essential, especially in the wake of capital liberalization.

Third, close regional cooperation is essential for the prevention and control of crises, especially among the emerging economies in Asia, since turbulence in one market can easily spread to the rest of the region.

These are the challenges which we must all address, together with the Fund and the Bank. The good news is that generally the Asian countries enjoy relatively good economic fundamentals. So, if lessons are learnt from the recent experience and the economy is managed properly, the emerging economies of Asia should continue to grow at a high pace in the future.

Role of the Fund and Strengthening its Function in the Wake of Capital Liberalization

Now to the role expected of the IMF in the wake of capital liberalization.

Today, integration of the financial markets and capital liberalization are already irreversible trends. These will ensure efficient distribution of resources and have a positive effect on economic growth. In promoting capital liberalization, the Fund should play a central role as the organization that oversees the international monetary system. In this context, the proposed amendment of the Fund Articles to make the promotion of capital account liberalization a specific purpose of the Fund is extremely significant. It is hoped that further progress will be made in the discussion on the amendment.

In view of the recent currency crises in various parts of the world, however, the risks associated with capital account liberalization must also be taken into account in drafting the

actual amendment. It is essential that the amended Articles have adequate levels of flexibility that will allow a response according to the size of the economy and the development stage of the financial market in each country.

On the other hand, we mustn't overlook the fact that in the wake of capital liberalization, each country more than ever is faced with the risk of being exposed to abrupt as well as large-scale capital movements. For the Fund to maintain stability in the international monetary system under such circumstances, it is essential that it strengthen its activities. To this end, a strengthening of the financial resources of the Fund is the necessary first step. For its part, the Government of Japan completed on September 8 the domestic procedures needed for the New Arrangements to Borrow (NAB) and has notified the Fund of our adherence. It is hoped that other member countries will also complete their domestic procedures so that the NAB will take effect very soon.

At the same time, we welcome the agreement on the Eleventh General Review of Quotas. However, as was evidenced by the recent financial support to Thailand, the financial resources of the Fund need to be enhanced further. For future reviews of quotas, we must take into account the expected magnitude of financial crises that might result from the liberalization of capital movements.

With regard to the allocation of SDRs, I welcome the latest agreement at the Executive Board of the Fund to make the first allocation of SDRs since 1981. The agreement is most welcome because it will achieve greater equity.

Furthermore, I believe it is essential that the Fund strengthen its surveillance of the economic policy and financial markets of each member country. The Fund is also expected to provide expanded technical assistance to help develop sound financial markets through strengthened supervision of financial institutions and increased transparency of their operations. These efforts are vital as they will translate into greater discipline in financial markets and more effective prevention of crises.

Sustainable Growth of Developing Countries

I will now touch upon what is needed to ensure sustainable growth of developing countries.

First of all, it is essential that they strengthen the base for further economic growth by modernizing industrial structure and developing infrastructure. For example, Asia has an enormous need for infrastructure development. Though the public sector will continue to play a significant role in this area, there is a limit as to what and how much the public sector alone can do. This is where multilateral development banks can play a significant role by promoting private capital flows for infrastructure development.

In this respect, I welcome the action program which the World Bank Group presented at this Development Committee in response to the proposal the Governor of Japan made at the last Annual Meetings. I strongly hope that the entire World Bank Group will actively implement the action program to deliver results on the ground.

For the same reason, it is essential to strengthen and expand guarantees of the World Bank Group. In particular, with its activities steadily expanding in recent years, MIGA needs additional financial resources to continue its activities. We welcome the agreement on the adequate level of MIGA's capital increase reached at this Development Committee, and at the same time strongly urge the MIGA Board and other relevant parties to come to closure on details of the capital increase before the next Development Committee Meeting in April, 1998.

Second, developing and strengthening financial and capital markets is vital for sustainable growth of developing countries. For these countries to fully benefit from globalization, it is essential that they win investor confidence and increase efficiency of their domestic financial markets by implementing financial reforms.

Developing and strengthening financial and capital markets are also indispensable to steadily facilitating private infrastructure development.

In the recent currency crisis in Thailand, the Bank played a key role. Thus, we strongly hope that multilateral development banks will make a comprehensive study and strengthen their activities in this field.

Third, poverty reduction and environmental protection are necessary for sustainable growth. In Asia, over 900 million people still live in poverty, accounting for about two-thirds of the world's poor; in Sub-Saharan Africa, over 200 million people live in poverty. In tackling this problem, it is essential to increase employment and income through sustainable growth, while emphasizing expanded measures targeted to these populations.

Many environmental issues require concerted efforts across borders. In this context, the Bank should be the forerunner among the multilateral development banks. In particular, the functions of the Global Environment Facility (GEF) should be strengthened. In formulating country assistance strategies (CAS), the Bank should also strengthen policy dialogue with each country to ensure that environmental policies are strictly adhered to medium- and long-term development strategies.

For its part, the Government of Japan stands ready to support such areas as promoting private capital flows, strengthening the financial sector, and fighting against poverty and environmental destruction by further utilizing the Japan Special Trust Fund in the Bank, entitled the Policy and Human Resources Development Fund (PHRD), based on further discussion with the Bank.

In Japan, we are more actively addressing global environmental problems such as global warming and acid rain. Regarding anti-pollution and global conservation measures, our government decided to ease ODA loan conditions to the level equivalent to those of the International Development Association (IDA). This policy was implemented this month prior to the Third Session of the Conference of the Parties to the United Nations Framework Convention on Climate Change (COP3) to be held in Kyoto this coming December.

Finally, continual effort to maintain development assistance is equally important. The Government of Japan intends to provide as much assistance as possible under the severe fiscal constraints, however, it is also necessary for the multilateral development banks to provide even more efficient and effective operations .

In this respect, the Government of Japan supports the framework of the Strategic Compact while, at the same time, urges the Bank to attach greater importance to efficiency of its activities.

Moreover, strengthened collaboration among multilateral development banks, other donors, the private sector, and NGOs is an effective factor for maximizing the aid impact. I believe it is important to fully consider a wider range of opinions on development issues, including the role of MDBs, to build support for development assistance.

Conclusion

Mr. Chairman:

Each country's circumstances are different. Each has a different industrial structure, and is at a different stage of development. Some economies are developed. Some are developing. Some are in transition. Yet others are emerging.

Despite such diversity, there is a possibility that we all might face a crisis of the type and magnitude never before experienced as the globalization and integration of financial markets proceed. Increased uncertainty associated with capital movements might also make our policy management even more difficult than it is now. These are the challenges we will have to address in order to ensure sustainable growth of the world economy.

One obvious way to address these challenges is to further promote collaboration among member countries. This is where the World Bank and the IMF can play a central role in coordinating concerted action through global as well as regional dialogue.

In closing, I strongly hope that the Annual Meetings in Hong Kong will provide an opportunity to confirm these commitments of ours and will allow us to go a step further in our collaboration.

Thank you.