STATEMENT BY THE GOVERNOR OF THE FUND AND THE BANK FOR MALAYSIA

Dato Mustapa Mohamed

More than a year has passed since the financial crisis unfolded in East Asia. Recent trends in global financial markets indicate that the international financial environment has further deteriorated. There is now a growing concern of the risk of a global financial meltdown. When it first unfolded, the Asian crisis was not recognized as a global problem requiring a global approach. While there is a general recognition of the risks in the global financial markets, the international consensus reached at these meetings for a rapid response to restore stability in the world financial system now needs to be translated into concrete outcomes. During last year's IMF/World Bank Annual Meetings in Hong Kong, my Prime Minister had raised many of the issues that have been the focus of the discussions at this year's meetings. In particular, this relates to the need for the reform of the architecture of the international monetary system to deal with the mounting destabilizing flows that are having a devastating effect on countries. These cautions are only receiving urgent attention after inflicting high costs to the global economy.

As we gather here in Washington, there is yet no clear sign of stability being restored. Indeed, this is the third time that we have gathered since the crisis. Several proposals have now been made to strengthen the architecture of the international monetary and financial system, but the world's financial leaders need to act decisively to bring these proposals to yield positive constructive results.

In the region, we have witnessed the devastating effects of destabilizing capital flows. Thailand, Korea, Indonesia, Malaysia, and other Asian economies have all fallen victim to the onslaught of speculative capital flows in search of higher returns. The crisis has spread to Russia and more recently to Latin America. The collapse of the mother of all hedge funds, the Long-Term Capital Management Fund, is a strong indication that no country is spared from the contagion effect of the present crisis. But for the fact that it could destroy the financial system of the very rich, the activities of the fund would have been overlooked. As it is, the possibilities of it causing havoc in the world's capital markets are finally receiving attention.

As more and more countries succumb to the contagion effects, the risk of a global financial meltdown has increased. The world economic situation has deteriorated considerably and the near-term outlook is more uncertain than ever. The IMF has revised global growth downward four times since December 1997. As we gather here today, the prospects do not look promising and the contagion effects show no sign of abating.

The experiences of the affected countries thus far clearly demonstrate that the traditional policy prescription has not produced results. In the case of Malaysia, the combination of high interest rates and tight fiscal policies further distressed economic activities and led to a contraction of the domestic economy. Nations have been impoverished by this approach, setting back decades of development and progress.

The international community's response to the crisis has been to call for reforms including improving transparency and governance. The argument is that lack of transparency and accountability makes it difficult for markets to function well. Various committees and working groups have been duly formed to study these issues as part of the move toward a modern architecture for the international monetary system. At this stage however, we need to chart the steps that need to be taken for the implementation to achieve this end.

Now after more than a year into the world's worst economic crisis, many prominent economists from the West have voiced concern over the approach that has been taken. There is a growing skepticism over the effectiveness and appropriateness of traditional ideas and orthodox policy prescriptions. There are also rising concerns on the destabilizing activities of hedge funds and other institutional investors and the lack of regulation over their activities. Of course, the reasons for the shift in stance has not been so much concern over the plight of the impoverished millions in Asia as much as alarm over the increased risks of global contagion, deflation, and loss of markets. Instead of reviving confidence, the IMF approach has inadvertently made a bad situation worse. The combination of sustained high interest rates and tight liquidity has led to a severe contraction in the real economy and a vast overhang of bad debt throughout Asia.

The traditional prescriptions backfired because the severe economic contraction that was precipitated by massive capital outflows was exacerbated by contractionary monetary and fiscal policies. In such an environment, foreign creditors became increasingly concerned that debtor firms would default on their loans. In addition, the actual official foreign financing fell short of expectations. Banks also came under extreme stress and, amidst concerns over the health of their balance sheets, began to slow down disbursement of new loans. Despite contractionary policies, flight to quality continued while regional currencies continued to depreciate.

The present framework of the global financial system was designed more than 50 years ago and is clearly inadequate to deal effectively with the risks and challenges of volatile capital flows. The framework, including the role and functions of the Bretton Woods institutions, needs to be reviewed urgently to keep pace with changing times. Closer cooperation between the World Bank and the IMF is needed to further strengthen their capacity to respond to the growing demands for assistance in the three key areas of financial, corporate, and social safety net programs. As had been pointed out by several speakers, particular attention must be paid to the social dimensions of adjustment measures by strengthening social safety net programs and protecting budget allocations aimed at helping the poor.

In such times of crisis, large resources are required by Fund and Bank members to refinance their economies. In this regard, the World Bank must fulfill the role mandated to it. Given that sourcing funds from the market would be extremely costly, I urge the Bank to fulfill this financing role and provide the much-needed assistance to preserve the socioeconomic gains made by these countries and to restore investor confidence. I am concerned that inadequate financial support from the World Bank would undermine reform efforts and aggravate human suffering.

The belief that globalization and liberalization of markets and the unfettered workings of the market, especially the financial market, can only bring benefits is flawed. In the haste to liberalize, the downside risks have been downplayed. The Asian financial crisis has negated this claim as the speed of financial liberalization and the huge amounts of capital flows have been proven as destabilizing and disastrous. Unbridled capital flows, including speculative capital, have wrought havoc on economies that have relatively underdeveloped and thin capital markets. More, rather than less, government intervention may in fact be needed to ensure that there is effective financial regulation and corporate governance.

Proposals for Reform

At last year's Annual Meetings in Hong Kong, Malaysia called for changes in the way the international financial system operates, suggesting the need to formulate international parameters for currency trading as a first step toward a review of the entire system. Our suggestion was dismissed as an attempt at "denial" and "blaming others" for our own problems and weaknesses. The failure to recognize that the crisis is, in fact, due to both external and internal factors has delayed efforts to deal comprehensively with all the issues that emerged from the crisis. More recently, as the crisis continued to engulf more countries, awareness is increasing of the need for the reform of the world financial system. We will risk a global meltdown if we continue with ad hoc and incremental measures. A complete overhaul of the international monetary system is required and required soon. Allow me at this juncture to propose that at a minimum, the reform of the system should include the following key elements.

First, increased transparency should not only be on the part of governments, but also on the part of financial market players. Currently, there is no regulatory authority to oversee the orderly functioning of the international capital markets, especially currency trading. The rationale for such an institution would be similar to that for a national regulatory authority that supervises the activities of domestic stock exchanges, and commodity and futures trading. The regulation of cross-border financial market transactions is not new. Work is already under way to address shortcomings in the international financial system so vividly highlighted by the Asian crisis. These include banking supervision that is being undertaken by the Basle Committee; the establishment of universal principles for securities regulation by the International Organization of Securities Commissions (IOSCO); and the development of strong global prudential standards in the insurance industry by the International Association of Insurance Supervisors (IAIS). A Joint Forum on Financial Conglomerates has also been set up by the Basle Committee, IOSCO, and the IAIS to develop a set of principles for supervising internationally active financial groups.

Second, the establishment of a mechanism for making rating agencies accountable for their actions is needed, particularly when their ratings have a significant adverse impact on a country, more than had been warranted by economic fundamentals. In recent times, it has been shown that rating agencies have failed to make objective assessments, despite being provided with comprehensive information. None of the rating agencies predicted the outbreak of the regional financial crisis. Indeed, they were bullish on Asia's prospects. Subsequently, when the contagion effects of the crisis became more apparent, the rating agencies exacerbated the situation by continually downgrading the credit standing of the affected Asian economies. The downgrades were often based on inaccurate assessments of the countries' economic and financial situations. This further undermined investors' confidence, precipitating panic selling by investors.

Next, it is time we set up an international lender of last resort. In addition to the need to establish a global regulator of world capital markets, it is also important to provide temporary liquidity support to economies in crisis facing problems of massive capital flight and a liquidity crunch. There is a need for a lender of last resort for countries that are fundamentally sound and financially solvent, but which require temporary liquidity support to weather a "run" on their economies.

Finally, there must be a review of the role of international financial institutions. The role of the IMF, World Bank, and other international financial institutions must be reviewed to ensure that they remain relevant to the changing needs of their members. In particular, closer collaboration among the international financial institutions, notably the IMF, World Bank, and the Bank for International Settlements are essential to ensure that the world's financial system continues to function smoothly. We should also consider the establishment of a global system for the exchange of information among the international financial institutions, international regulatory bodies, and home authorities. Such a system of global information sharing would provide important early warning signals of impending crisis and enable the affected countries and the international community to undertake appropriate policy responses.

We remain convinced that an international consensus on the reform of the international monetary system is the preferred option to address the present and future financial crisis. No country can do it alone. Efforts by countries such as Malaysia, Hong Kong, and Russia represent only short-term measures to cope with the immediate problem of volatile capital flows. A permanent, multilaterally agreed solution is required to strengthen the international financial system.

In the interim, what are the options available to developing countries like Malaysia? Malaysia, like other affected economies, has persevered since the crisis began one year ago to undertake macroeconomic adjustment policies and implement financial reforms to reduce the risks and vulnerabilities arising from external developments. These measures were aimed at achieving macroeconomic stability and increasing the resilience of the financial system. As the economy slows down, strains are increasingly being felt in the financial system.

Malaysia's Exchange Control Measures

In the past year, Malaysia has suffered a considerable loss in income and wealth. No country that has experienced a 40 percent depreciation in its exchange rate and a 65 percent decline in stock prices can withstand the dislocation in its economy and the social costs it entails. In an effort to ensure prospects for stability, Malaysia has introduced selective administrative controls to allow for orderly capital flows and insulate the domestic economy from such external risks. It is emphasized that the new controls are not a substitute for sound macroeconomic and financial policies. The measures will provide some breathing space to ensure that the ongoing structural adjustment measures can continue uninhibited by external developments. The government is in fact on course in its efforts to restructure the financial sector, in particular, the recapitalization of the financial institutions. The measures are also aimed at preserving the gains that have been made in terms of strengthening the balance of payments position and in terms of containing inflation to create a positive environment to support economic recovery.

These measures are by no means radical. The measures are not even unique. Indeed, a large number of both developed and developing countries have imposed capital controls. It was only by mid-1995 that all industrial countries removed exchange controls on both inflows and outflows of capital. Countries such as Germany, Switzerland, and the United States reimposed capital controls when they faced difficulties in achieving domestic and external balance in the postwar years. Even as recently as 1992, Spain taxed certain short-term transactions and temporarily tightened controls on onward short-term capital movements, arising from the aftermath of market disturbances within the ERM of the European Union. Capital controls played an important part in the defense of the Irish pound, the Portuguese escudo, and the Spanish peseta in the 1992 ERM crisis. And among the developing countries, Argentina, Chile, Mexico, Venezuela, and China have also used capital controls.

I would like to assure the international financial community that the imposition of these exchange control measures will not affect the business operations of traders and investors or the normal conduct of economic activity. We continue to guarantee general convertibility of current account transactions and the free flows of foreign direct investment, repatriation of interest, profits, dividends, and capital. Indeed, the changes are intended to contain the potential for speculation on the ringgit and preventing excessive cross-border flows of short-term capital.

As the changes in the exchange control rules are directed at containing speculation on the ringgit and at minimizing the impact of short-term capital flows on the domestic economy, they will not affect the normal conduct of economic activity. More important, the measures continue to guarantee:

- the general convertibility of current account transactions;
- the free flows of foreign direct investment; and
- the free repatriation of interest, profits and dividends, and commissions.

As the new rules were aimed at containing speculation on the ringgit, they will have no impact on nonresidents who are Malaysian individuals with permanent resident status residing abroad, foreigners studying and working in Malaysia, embassies, high commissions, consulates, central banks, international organizations, and missions of foreign countries in Malaysia.

To reiterate, Malaysia is not closing its doors to the foreign investor community, much less to the international economy. Malaysia still maintains general current account convertibility and is not resorting to any rationing of foreign exchange. Beyond that, Malaysia has not changed its policy on foreign direct investment and repatriation of profits and dividends from foreign investment. We also wish to emphasize that we remain fully committed to making all external debt payments, in full and on time, and that foreign exchange is freely available for such payments. The Malaysian economy is a very open economy. Trade as a percent of GNP will remain high, exceeding 170 percent, foreign direct investment of more than 20 percent of total private investment, and foreign market share in total assets of the banking system of about 30 percent.

The recent measures are aimed at creating stable domestic conditions to promote economic recovery with price stability. In the interim period, the measures will strengthen Malaysia's economic fundamentals in order that we can better manage the challenges of the globalized financial markets. Toward this end, Malaysia remains committed to pursuing structural adjustments in the economy in general, and the financial sector in particular. These adjustments are necessary and important to protect long-term investments in Malaysia. Reflective of the commitment to direct foreign investments, existing measures will continue to guarantee free flows of long-term capital.

These selective administrative controls were implemented to insulate Malaysia from adverse external developments. These measures will remain in place for as long as there is no regulatory framework for financial flows. In the absence of such a framework, it is unlikely that financial stability will be restored.

In conclusion, we hope that the international community will evaluate Malaysia's measures fairly. Malaysia remains committed to the trade-oriented open market that has served us so well for over 30 years. However, extraordinary circumstances have led us to implement these measures to insulate Malaysia from contagion developments in the global financial markets. The more fundamental issues of the global system, however, remain. A solution to these issues can only be achieved through the concerted efforts of the international community. These efforts would increase the prospects for a permanent solution to restore stability in the international financial system.

Statement by the Governor of the Bank for Malta

John Dalli

It is certainly an honor for me to address the Annual Meetings of the International Monetary Fund and the World Bank. Before I express my views on some of the current economic and financial issues, I would like to join other Governors in extending a warm welcome to the Republic of Palau as a new member of the Bretton Woods institutions.

Since last year's Annual Meetings, the prospects for world economic growth have weakened considerably in the wake of the Asian financial crisis, which continues to have negative reverberations for both industrial and developing countries. Forecasts for world economic growth in 1998 have been revised downwards, to about the 2 percent level, and there is a possibility that next year's economic expansion could fall as low as 1 percent. Unfortunately, it appears that the contagion effects of the Asian crisis have not been sufficiently contained, and so their dampening impact on global economic growth could be much stronger than originally anticipated. From my country's perspective, that of a small island in the Mediterranean, the global economic slowdown is viewed with concern, given the openness of our economy and its vulnerability to external forces. Economic activity in

Malta is heavily dependent on external demand, particularly its export markets in Western Europe. Our main preoccupation is the fact that, while the risk of a sharp economic contraction in Western Europe is unlikely to materialize, there is a strong possibility that fiscal and monetary policies in that region will be maintained on a tight rein. This may prevent domestic demand in the euro-area countries from expanding sufficiently to offset the adverse impact of a protracted slowdown in other regions of the world.

One of the implications of the financial turmoil in East Asia has been a review of the role of the IMF and the World Bank in the international financial system and the ability of these two institutions to address the current financial crisis which threatens to destabilize the system. We do believe that in the difficult circumstances of the past year both the Fund and the Bank have shown effectiveness in dealing with the crisis and the necessary flexibility to deal with the internal problems of the countries concerned. However, in the light of the global repercussions of the crisis and the ongoing contagion effects, we feel, as has already been acknowledged in international fora, that there are shortcomings in the architecture of the international monetary system, and these have to be addressed on the lines suggested by the IMF's Executive Board and endorsed by the Interim Committee last April. The novelty of the proposed measures is that they will involve the cooperative efforts of the entire international community, including the private sector.

The measures, in fact, highlight a number of important aspects, notably the need for a strengthening of domestic financial systems. No doubt, the weakness of the financial system in a number of countries has been one of the factors that has contributed to the international financial crisis. In today's global market, which is characterized by the rapid movement of short-term capital flows, it is very difficult for a country to avoid a disruption in its macroeconomic performance if it does not have a sound financial system. Consequently, the emphasis that the Fund, together with other organizations, will be giving to helping members better design their financial sector and their supervisory and regulatory systems is certainly warranted.

In Malta, over the past decade we have strengthened the institutional structure of our financial sector with the aim of establishing the island as a sound and efficient international financial center. At the same time, we have allocated substantial resources to the development of a strong supervisory system that closely monitors the financial sector as a whole in order to ensure its stability and its compliance with international standards and practices. We have set up a separate regulatory authority to supervise all financial sector activities except banking, which remains the responsibility of the central bank. The bank, in fact, has ensured that almost all core principles recommended by the Bank for International Settlements for effective bank supervision have been implemented over the past year. Here, I would like to mention that an IMF mission on banking supervision, which visited Malta less than two years ago, expressed its satisfaction with the high standards of our regulatory regime. I am therefore happy to say that, so far, our system of financial sector supervision has worked satisfactorily and the volume of international financial business undertaken by the sector has been increasing steadily.

The importance of strengthening Fund surveillance has also been stressed. All member countries have the responsibility to pursue prudent macroeconomic policies, but this responsibility assumes even greater importance when those countries that have a significant impact on the international monetary system are involved. This notwithstanding, I believe that a strengthening of the surveillance role of the Fund should apply to all countries, regardless of size, with consultations between member countries and the Fund taking place more frequently, possibly on a more informal basis during the period between the visit of one Article IV consultation mission and another. My country had requested such an arrangement and recently experienced these informal consultation meetings with Fund officials. These meetings proved to be very useful for economic policy decision makers at the national level. As regards the proposal by the Fund that more information should be released after Article IV consultation missions, while we have no objection to the issue of Public Information Notices, we still believe that staff reports should only be published at the discretion of the member country. As has been apparent from discussions on this issue, there is a possibility that officials in many countries may be discouraged from cooperating fully with Fund missions for fear that their confidential remarks and statements on the state of their economy will be disclosed publicly.

However, I would like to emphasize that my country fully supports the Fund in its efforts to enhance the standards of economic and financial data published by members, especially where this is related to the core indicators. Malta is presently adhering to the General Data Dissemination System (GDDS) to ensure that high-quality standards are achieved for the full range of economic, financial, and sociodemographic data. As we continue to reform and upgrade our statistical resources at the national level, we intend to use our participation in the GDDS as a step toward subscribing to the more demanding Special Data Dissemination Standard.

Another important initiative taken by the Fund concerns government transparency and accountability. The Code of Good Practices on Fiscal Transparency adopted by the Interim Committee in April serves as an effective guide for members on fiscal management. In countries where the public sector looms large, the provisions of the code are all the more relevant. In Malta as well, the impact of the public sector on the economy is quite significant, and it is our intention to gradually reduce its size through—where possible—the transfer of certain economic activities to the private sector and cooperative schemes, and also through a privatization program. Within the public sector itself, we will be introducing measures to streamline resources and improve efficiency. Where fiscal matters are concerned, we will introduce proper budgetary planning techniques and better financial management to ensure that the fiscal deficit as a percentage of GDP does not exceed internationally accepted levels. In coming years, we hope as much as possible to implement all the provisions of the code and would certainly welcome technical assistance from the Fund to achieve this objective.

Another important issue is capital account liberalization. Over the past year, the Fund remained committed to capital account liberalization notwithstanding the fact that massive capital flows have been a major factor contributing to the Asian crisis. At the IMF seminar on this subject earlier this year, however, there was a general consensus that policies aimed at the liberalization of capital movements had to be orderly and well sequenced. In addition, they had to be implemented only when the appropriate macroeconomic and exchange rate policies were in place and when the financial system was sound. More significantly it was recognized that the pace of liberalization had to be adapted to the circumstances of individual countries. This is certainly our view on the issue, although we do not object to an extension of the IMF's jurisdiction on capital movements as long as this is expressed in general terms. My country is fully aware of the benefits of an open and liberal system, and its decision to accept Article VIII status almost four years ago was taken with this objective in mind. In subsequent years, we gradually removed a number of restrictions on both inward and outward capital flows, and it is our ultimate goal to remove them completely over the next few years. This strategy course will, in fact, be consistent with our desire to join the EU as soon as possible, as an important condition of membership of the EU is the full liberalization of the capital account.

With its strong commitment to EU membership and its desire to participate in the next phase of EU enlargement, Malta will continue to pursue vigorously policies aimed at further reforming and liberalizing the economy. At the same time, we are monitoring closely all developments that are taking place in the EU, particularly those that are related to European Economic and Monetary Union and the single currency. Apart from our membership objectives, the establishment of European Economic and Monetary Union is expected to have important implications for our economy, given our very close financial and trade links with the countries that will be participating in the union. European Economic and Monetary Union is certainly a historical event and is expected not only to have a profound impact on international financial markets, but also to have important implications for the way the Fund carries out its operations and conducts its surveillance.

Here, I would like to reiterate my country's strong support for the valid work undertaken by the Fund and the Bank at a time of serious financial problems in the global economy. We believe that Bank-Fund collaboration, particularly in the field of second generation reforms, has to be maintained and strengthened to enable the two institutions to respond effectively to crises that threaten the stability of the international financial system. In this regard, it is important that both institutions have the financial capacity to carry out their operations. In the case of the Fund, the potential resources available under the Eleventh General Review of Quotas will substantially strengthen the Fund's liquidity position. It is necessary therefore for members to approve the Eleventh General Review of Quotas as soon as possible so that this will come into effect before January of next year. I am happy to say that despite its limited resources my country has completed all procedures in connection with the quota increase and has also approved the Fourth Amendment of the Articles of Agreement that will enable the Fund to effect a special one-time allocation of SDRs that would ensure that all participants in the SDR Department will receive an equitable share of cumulative allocations. Malta also gives a modest contribution to the resources of the ESAF and the HIPC Initiative.

In conclusion, I would like to thank the management and staffs of the Fund and Bank for their continued support and wish them all success in their operations. Through Fund technical assistance in recent years, we have been able to implement important reforms in our financial markets and in our banking system. Recently Fund assistance has also been forthcoming in the important area of government finance statistics. Finally, I would like to express my country's appreciation of the assistance and advice that is provided throughout the year by the Executive Directors who represent Malta on the Boards of the Bank and the Fund.

Statement by the Governor of the Bank for the Marshall Islands

Tony Debrum

I wish to thank the people and the government of the United States for hosting this year's Annual Meetings. Unlike last year's meetings, where cautious optimism prevailed, this year great fears have arisen. These fears encompass both the future of global capitalism and, indeed, the future of the World Bank itself. The Marshall Islands also shares these fears.

Micronesia's Status

The countries of Micronesia constitute a very small percentage of the world's economy. However, our unique location in the center of the Pacific

Ocean provides us with an excellent vantage point to observe and maintain a partnership with both Asian countries and the Americas. We are in the middle of nowhere, yet we are also in the middle of everything.

Our current economy was initially formed based upon grants and reparations from the United States. More recently, we have received loans and grants from the Asian Development Bank. This has not been a pain-free structuring. Our past dependence upon government employment has led to reductions and increased unemployment. However, in the past decade, the value of our fishery industry has been recognized by Asia, North America, and Europe. It is our goal to see that this resource is not plundered or undersold. With the help of our friends in Australia, the South Pacific Forum, and North America, we are succeeding in this goal. We believe that our fishery industry will provide sustainable economic growth and related employment for our citizens.

The Marshall Islands is in a unique situation. Our economic development is at the stage of a developing nation, yet we have unfettered access to the United States. Our currency, by treaty, is the U.S. dollar, and we do not suffer the fear of massive currency devaluation. The access to the United States has allowed a number of our citizens to enjoy the benefits of education and employment within the United States. This creates an abnormality; our resident citizens can see the benefits of successful capitalism yet live in what is perceived as a third-world environment.

The economic benefits of living in a developed nation, once enjoyed, cannot be dismissed. It is with this in mind that we share the deep concern of our cousins in Malaysia and Indonesia. Seemingly overnight, their prosperity has vanished, replaced with fear and suffering. While a macroeconomist can analytically describe a negative growth rate, the suffering of the people in the affected nations cannot be adequately described.

Observations

Looking to the East and to the West, we have great concerns. We see the potential for instability and uncontrolled nationalism. Being a small country, we are continually amazed at the lack of understanding and bureaucracy of the world's economic organizations. Currently, everyone agrees that a "contagion" exists, yet no one seems to have answers. The remedies that historically worked for western nations are not working in an Asian environment. The World Bank meets and makes fine-tuning adjustments, the Group of Seven meets and announces its optimism, and the United States announces new reforms and goals. Yet, the "contagion" continues, with Russia in default and South America unstable. Furthermore, the greatest minds in economics cannot seem to agree on a proper and achievable solution.

This situation can only lead to provincial thinking and political and organizational blame. Faultfinding is greatest once a crisis has been identified. While the Marshall Islands is somewhat insulated from this crisis, we wait impatiently for some consensus (some form of leadership) to pull the world together. The time wasted in assessing blame will only ensure that the problem grows.

Frankly, in my week here, I have witnessed a variety of speakers expound on theories that only create so much hot air. I fear that many of our experts on economic theory have become so enamored with the past successes of the economy that they are empty shells when dealing with adversity. It is surprising that in my week here the most interesting article I have read describing the economic situation and possible solutions was not from a noted staff member of the World Bank, but from the former U.S. Secretary of State, Henry Kissinger. He eloquently stated that the role of politics in economic reform cannot be overstated and has been seemingly overlooked in the past year. We urge our colleagues not to confuse capitalism with democracy.

We live in a time of instant communications, making us truly global in the delivery of bad news. What the world needs is not technical discussion of stock indexes, capital flows, or projected GNP, but reassurance. In short, if the "contagion" is to be controlled, decisive leadership must be shown. The question I raise with the Bank and to my fellow Governors is, "are we capable of providing that leadership?" If not, then who is, and how can we assist them?

STATEMENT BY THE GOVERNOR OF THE BANK FOR MONGOLIA

Bat-Erdene Batbayar

It is a great pleasure and honor to address the Bretton Woods institutions' Annual Meetings, representing Mongolia, a country with a population of 2.4 million, a deep historical heritage, and abundant natural resources. Let me bring to you warm greetings from the government of Mongolia and the Mongolian people.

This year's Annual Meetings are of great importance to the world when almost 40 percent of the global economy is experiencing economic recession and many countries are affected by severe financial crisis and turmoil. This international forum that pools the world elite provides all of us with an opportunity to share thoughts and views on problems and outstanding issues we face and jointly seek ways of resolving them.

Today Mongolia is irreversibly undergoing an ambitious agenda to transform the whole political, economic, and social institutions into a democratic, humane civil society based on a market economy and the rule of law. The country is relatively successfully weathering the adverse effect of contagion triggered by the financial turmoil in Southeast Asia and maintaining the momentum to make its economy prosper and to improve the well-being of the Mongolian people.

Mongolia has successfully been implementing the midterm ESAF-supported program agreed with the IMF in 1997. For the first eight months of this year, annual inflation fell to 7.5 percent, down from 55 percent in the same period in 1997 and from 325 percent in 1993. Real GDP rose to 3.9 percent in 1997 from 2.6 percent in 1996 and is projected at about 3.5 percent in 1998. International reserves stood at $118 million by end-June 1998, equaling 12 weeks of imports against $102 million for the same period last year. The exchange rate has been relatively stable for the past three years. The unemployment rate has been decreasing, compared with that of last year.

I would like to stress the fact that these achievements have been made possible thanks to the support and assistance of international financial institutions such as the IMF, the World Bank, and the Asian Development Bank, as well as our bilateral donor countries. The prescription of policy measures designed by the IMF to overhaul the country's economy has proved its correctness while producing positive outcomes. Today we are negotiating with the IMF the second-year program under the ESAF.

Notwithstanding, Mongolia is still ranked among developing countries with $400 annual per capita income and a growing challenge of poverty. The country's economy is very volatile and imbalanced, relying mainly on a few manufacturing industries compounded by a rapidly worsening external environment. The banking sector is still weak financially, operationally, and in terms of skilled human resources. The government budget is under high pressure triggered by a continuing decline in international market prices of major export items such as copper, gold, and cashmere, troubled state-owned banks, ineffective and fully subsidized social welfare and security institutions, and a shortfall in projected privatization receipts. Infrastructure remains underdeveloped and is far from meeting the basic needs of the population and businesses. Technology is greatly outdated and environmentally unfriendly. The private sector is still weak and nascent. At present, the public sector constitutes a large segment of the economy. The country lacks access to the international markets and has a shortfall in competitiveness, in addition to a landlocked, isolated, and unfavorable geographical location. Unemployment and poverty threaten to grow unless appropriate policy measures are undertaken, and necessary funding secured.

The current global trends and the existing situation in the economy dictate that Mongolia focus more on maintaining momentum and positive developments produced while strengthening economic fundamentals in order to be ready for and prevent possible danger associated with regional and global economic crisis and turmoil. Mongolia is not fully immune to their perverse epidemic impact.

The government of Mongolia is eager to complete transition in a relatively short period of time with less economic and social costs. This will require well-grounded, carefully elaborated policy and implementation tools backed by substantial capital, human, and intellectual resources. Constructive cooperation with the international financial institutions, including the IMF, the World Bank, and the Asian Development Bank, will no doubt help to attain this important mission.

We have witnessed growing partnership and cooperation with the World Bank Group based on the spirit of mutual understanding, trust, and respect for each other since 1991 when Mongolia joined the Bretton Woods institutions.

The World Bank is providing worthwhile assistance to Mongolia to rehabilitate and sustain its infrastructure, stabilize its macroeconomy, enhance structural reforms, and alleviate poverty. Since 1991 the Bank has funded 10 development projects worth about SDR 167 million. We also greatly commend and highly value the Bank's nonlending program provided to Mongolia. The Bank plays a vital role in coordinating activities in the Mongolia Assistance Group and, to date, has contributed to six successful Consultative Group Meetings co-chaired with the government of Japan. Foreign direct investment promotion is another important area of the Bank's intervention. Two successful international investment conferences in the areas of mining, oil and gas, agroindustry, and tourism have been convened in the past two years in Mongolia, and the existing legislature related to foreign direct investment has been largely improved under the umbrella of these two international forums.

The opening of the World Bank Resident Mission for the first time in Mongolia has opened a new chapter in the history of partnership relations and cooperation between Mongolia and the World Bank. It greatly contributes to the growing efficiency of Bank-funded projects and improved policy dialogue and coordination between the government and the Bank.

The government of Mongolia is keen to broaden collaboration with IFC, MIGA, and other agencies of the World Bank Group in private sector development, the promotion of foreign direct investment, and enhancing the country's competitiveness. Recently, Mongolia has become a full member of MIGA, which enables Mongolia to extensively work on investment promotion, applying tools that MIGA possesses.

Given the progress that has been attained in economic and social development and the satisfactory status of the projects funded by the World Bank, the government of Mongolia seeks an increase in annual capital allocation for Mongolia from its current level of $25–30 million within the context of the four major areas, such as macroeconomic stabilization, infrastructure development, structural adjustment, and poverty alleviation, agreed under the Country Assistance Strategy with the Bank. On our part, we will exert every effort to improve the efficiency and effectiveness of utilization of development funding.

In general we agree with the idea of overhauling the Bretton Woods institutions for the sake of increased efficiency, effectiveness, and a client-oriented approach. We believe that the IMF and the World Bank can play a vital leading role in addressing the pressing problems and burning issues associated with disastrous economic and financial crisis that evolves with a rapid pace touching upon many regions and countries.

I hope that this Annual Meetings will be a turning point in halting the global financial crisis and rehabilitating those economies in trouble, supplemented by a restoration of investors' confidence and fixing the ailing banking system.

I would like to reaffirm our government's commitment to economic reform and its strong willingness to take an active part in the important mission of the international community in its efforts to foster a stable environment conducive to global growth and the equal development of all nations worldwide toward the new millennium of humanity—the twenty-first century.

Statement by the Governor of the Bank for Morocco

Fathallah Oualalou

It is a pleasure and an honor to deliver this speech in the name of Arab Governors to the World Bank and International Monetary Fund meetings. Allow me, at the outset, to extend my heartfelt congratulations to you for being selected to chair the Board of Governors this year, Mr. Chairman.

Today, the global economy is going through a difficult phase, fraught with risks and challenges. The economic conditions in the Asian crisis countries and Japan have worsened; economic growth in those countries has deteriorated more than was expected. The crisis has spilled over into other countries, including Russia, where economic problems have clearly been compounded, and Latin American countries, where financial market fluctuations have so intensified that some of them were forced to take protective measures to limit the adverse effects on their economies. The speed of such developments and the potential worsening of the crisis on a global level have stressed the urgent need for concerted efforts by international financial institutions, member states, and the private sector in order to prevent further deterioration of the global economy and avert a spillover of the crisis into other regions of the world.

At this juncture, the world community faces several challenges. First is the need for concerted efforts to boost global demand and increase the growth rate of the global economy. This specifically means that high growth rates of the European and U.S. economies should be maintained, and Japan's economy should be revived expeditiously. The substantial decline in Japan's GNP growth in 1998 suggests the need to take more effective steps to stimulate the economy, proceed with banking system reforms, and solve the problems which prevent restoration of investor and consumer confidence in the possibility of reviving the economy in the near future. The world community should also take the steps necessary to prevent a spillover of the crisis into other countries.

The second challenge lies in the need for developing and emerging-market countries, especially Asian countries going through the current crisis, to persist in implementing the structural reform of their economies, and adopt prudent financial policies in order to successfully put in place the sound fundamentals that will enable them to restore their capacity for growth and prosperity. It is appropriate in this respect to commend the reforms undertaken by the Asian crisis countries amidst extremely difficult conditions. Those reforms have yielded positive results, which herald the beginning of improvement of their economic conditions. The IMF should also be commended for its flexibility in introducing changes in the reform programs of the crisis countries that would allow the expansion of social safety nets, and provision of the resources necessary to alleviate the burden of economic reforms on low-income groups.

The third challenge lies in identifying the causes of the recent crisis to determine the steps necessary to resolve them and prevent a recurrence in the future. This includes the need to identify weaknesses in the structure of the global financial system that helped to compound the crisis and spread its effects across countries. In this respect, it should be particularly noted that the crisis had shown the danger involved in the growing dependence on short-term capital flows to finance countries' external needs. The growing size of such flows intensifies the impact of their sudden decline on the stability of the banking sector in particular and the overall economy in general. Therefore, it is imperative to monitor private sector and state indebtedness and take measures to reduce dependence on short-term capital. The crisis has also shown the utmost importance of supervision of the banking and financial sector to ensure its soundness and stability in the face of the problems created by the sudden decline in banking system cash liquidity. The unexpected decline in capital flows to the Asian crisis countries, and the accompanying sharp drop in exchange rates and sharp rise in interest rates, revealed the weakness and fragility of many banking systems and the lack of adequate supervision of such systems. This accelerated the deterioration of their financial conditions and intensified the spillover of the effects of the crisis into various sectors of the economy. This calls upon us to support intensified efforts by the IMF to enhance the performance of the financial and banking sector in developing countries. This will enable those countries to take better advantage of the current globalization of the world economy and limit its risks.

The lessons drawn from the recent crisis prompt us to stress the importance of the deliberations by the Fund's Board on the liberalization of the capital accounts of member states and the conclusion reached during those deliberations that developing countries should exercise caution as they liberalize the movement of capital flows and that the soundness of the financial sector and rigorous supervision thereof should be ensured before capital accounts are liberalized. The deliberations also emphasized the advisability of giving priority to the promotion of direct investments and long-term capital flows before the door is opened for the movement of short-term capital.

Drawing lessons from the recent crisis, we also welcome the efforts of the IMF in several other important areas with a view to strengthening the international financial system. We support the Fund's steps to enhance the transparency of economic data, both those made available by official agencies in member states and those pertaining to the private sector, in order to help investors in financial markets assess the risk and alleviate the herd behavior that characterizes capital movements, especially when a crisis develops. We also welcome the Fund's growing interest in developing and disseminating internationally accepted standards in collaboration with other international financial institutions, while stressing the need to take into account differences in the conditions of member states and their effect on their ability to adopt such standards. In this respect, I would like to point out the importance of strengthening the Fund's capacity to act as advisor in this area, by providing necessary technical assistance to help member states disseminate and apply the standards that fall within its field of competence.

We also welcome the attempt to find appropriate ways to involve the private sector in reducing the possibility of future financial crises and in sharing the burden of resolving them when they occur. In this respect, we would like to stress in particular the importance of creating a mechanism to reschedule the external debt of the private sector in an orderly manner in intractable cases that cannot be solved by market forces. We also stress the need for authorities in capital-exporting countries to strengthen supervision of international operations of their financial institutions and to urge those institutions to publish adequate financial statements pertaining to such operations.

Amid growing disturbances in the global economy and the increasing role of the IMF in dealing with and limiting the adverse effects of recurrent crises, we cannot but stress the need to provide the Fund with necessary resources to carry out its mission. Therefore, we caution against the substantial reduction in the Fund's liquidity last year and call for acceleration of measures to adopt the agreed increase in members' quotas.

While we should focus in this Annual Meeting on the current problems threatening the stability of the global financial system, we should also not fail to note the urgent need to strengthen the international support of the initiative to reduce the debt of low-income countries (the HIPC Initiative). On this occasion, we express our support of this noble initiative in view of its importance in improving the conditions of those countries, and stress the need to provide the remaining funds required, either through bilateral contributions or through the sale and investment of a limited portion of the IMF's gold reserve.

In the course of dealing with debt problems, we would like to stress the need to find appropriate ways to resolve the debt problems of middle-income countries as well, since the debt burden is hindering development efforts in many of those countries.

Allow me now to move on to welcome the historic step anticipated early next year, namely the establishment of the European Economic and Monetary Union. While we wholeheartedly welcome this union in view of its expected benefits to the peoples of member states, we think that it is necessary to strengthen the role of the Fund in monitoring and supervising the economic and financial policies of the European community in view of the projected effects of the union on the world economy, the economies of neighboring countries, and those of the Mediterranean countries in particular. On this occasion, we would like to urge member states of the European community to reduce customs and tax restrictions on products of developing countries in order to minimize the potential adverse effects of the European Economic and Monetary Union on those countries.

I would like now to move on to issues related to the World Bank Group. The most important feature of World Bank Group operations in the past fiscal year was a substantial increase in loans and credits, far in excess of planned operations. Undoubtedly, the key factor that led to this level of activity was the role played by the World Bank Group in response to the financial crisis, particularly in East Asia, a role that should be supported in view of the wide-ranging effects of this crisis on the economies of many other countries.

We also welcome the continued focus of Bank operations on reducing poverty, developing human capacities, including health and education sectors, and protecting groups most vulnerable to the adverse effects of adjustment measures. We also look forward to increased attention to the conditions of low-income countries and those suffering the effects of armed conflicts. We would like to mention that there are broader areas for World Bank Group activities in the Arab countries, especially in light of the profound changes in economic policies undertaken by our countries in recent years, which have clearly contributed to the creation of an investment-friendly climate.

A look at the policies of the World Bank Group clearly indicates that the difficult circumstances through which the global economy is going will require more efforts to improve the ability of this Group to deal with fluctuations and complex situations resulting, in particular, from globalization and the adverse social and economic effects of financial crises.

We welcome the efforts exerted by the World Bank Group in the past fiscal year in this direction in the context of the Strategic Compact, the priorities it has adopted to improve the efficiency of performance and deal with the challenges posed by globalization and financial crises, and the emphasis on development of human capacities and broadening of cooperation with other institutions and donor countries. We also support the positive directions of World Bank Group practices designed to give borrowing countries the initiative in leading the development process and assist them in selecting and applying appropriate policies to support their development efforts.

We would also like to stress the need for the World Bank Group to focus on its main goal of reducing poverty and contributing effectively to the development process in a large number of low-income countries whose conditions have worsened in light of current global developments. This will require that the World Bank Group devote its limited resources to the main objectives consistent with its mandate and character, and to shoulder a limited portion of the burden of dealing with international financial crises in a way consistent with its financial conditions.

As is well known, the issue of fair burden sharing emerged also in the recent measures taken to deal with a decrease in the net income of the IBRD, which resulted in an increase in borrowing costs. We support the efforts made by Bank management and Executive Directors to analyze and discuss the projected decrease in net income and its potential effects on Bank activities. However, we believe that it is not fair that borrowing countries should shoulder the larger part of the burden of solving this problem, particularly since many loans recently extended by the World Bank Group were designed to stabilize world financial markets and also will benefit major industrial countries.

Therefore, we support the Bank management's initiative in calling for the establishment of a special fund to be financed by the donor countries to contribute to operations to be financed also from net income. In this respect, we also look forward to greater efforts by the major donor countries to replenish the resources of the IDA and provide additional resources to finance the HIPC Initiative. This would help alleviate the Bank's financial burden and ensure expanded utilization by low-income countries of World Bank Group resources.

Allow me now to move on to a brief review of current developments in the Arab countries. In this respect, it should be noted first that the continued decline in world oil prices has adversely affected economic growth rates in our region, particularly in the oil-exporting countries. This has resulted in a reduction in public spending and the adoption of measures to increase non-oil revenues of those countries. The oil-producing countries have intensified their efforts to diversify their economies by improving the investment climate for the private sector and enhancing the quality of education and training of the local manpower.

In other Arab countries, the implementation of ambitious economic reform programs continued. This resulted in higher growth rates and lower inflation in a number of these countries. Marked progress has also been achieved in transforming their economies to market economies by opening infrastructure to private sector participation and privatizing public enterprises. This progress has been reflected in a marked improvement in the economic climate in Arab countries, increasing the volume of private sector investment in various economic activities. However, it should be noted here that Arab countries have been adversely affected by a decrease in world capital flows, which in turn has adversely affected their development plans. Therefore, we appeal to the IMF and the World Bank to continue and to intensify their efforts to provide financial support and technical assistance to the Arab countries and their specialized agencies to enable them to deal with the challenges of globalization of the world economy and to maximize the benefits from the new international conditions. It should be mentioned in this respect that sanctions imposed or threatened against a number of Arab countries, which we have drawn attention to in the past, are still in place. This adversely affects the economic conditions of these countries. We can only reiterate our just request to reconsider those measures objectively in order to alleviate the suffering of the affected peoples. We raise this issue because of the adverse effects of those measures at the financial and economic level and on free trade and the free transfer of capital. Hence, we call on the IMF and the World Bank to play a role in this respect.

We would also like to note the distinct efforts made to develop the Palestinian economy and to build economic and financial institutions in the Palestinian territories. This has taken place with effective support from the World Bank, the IMF, and donor countries. We would like to commend these valuable international efforts which are designed to help the Palestine National Authority overcome the difficult economic and living conditions in the Palestinian territories. But we are sorry to note that such efforts still face mounting obstacles as a result of the Israeli practices related to continued blockades which have hindered the Palestinian people’s self-development efforts, wasted Arab and international financial contributions, and hampered the Mideast peace process. Therefore, we urge the World Bank Group, the IMF, all international institutions, and member states to demand that the Israeli government abstain from such practices and stop closing the borders and placing obstacles in the way of Palestinian, Arab, and international efforts to develop the Palestinian economy.

STATEMENT BY THE GOVERNOR OF THE BANK FOR MYANMAR

U Khin Maung Thein

First of all, on behalf of the Myanmar delegation and on my own behalf, I would like to express my warm appreciation to the Chairman on his assumption of the Chairmanship of the 1998 Annual Meetings of the Fund and the Bank. I have no doubt that under his able guidance, these meetings will be a great success.

As we gather here for the Fund and the Bank Annual Meetings, we are aware that the Asian financial crisis of 1997 and its contagion effects are very much still with us today. The course of events has shown how the Fund and the Bank have risen to the occasion by responding with prompt action to contain further deterioration of the situation, restore confidence, and help to lay the ground work to resume the road back to stable, sustained growth.

In the midst of the Asian financial crisis, it was found that the Fund has been striving to restore macroeconomic stability and market confidence through forceful structure reforms. While reviewing the Fund's activities for the past year, the Fund extending its interest to such new areas as good governance, strategy to fight corruption, and need for greater equality of economic opportunity, has caught our attention. Since the promotion of these activities has a direct bearing on quality growth, it has our whole-hearted support.

We have followed with appreciation the World Bank's financial supportive role in joining the Fund in dealing with the Asian financial crisis. We are also appreciative of the Bank's involvement in helping poverty reduction, enhancing the quality of life, and promoting sustainable environmental management.

In the light of the changes taking place in the international financial system and the increasing demands for the services from the Fund and the Bank, we hope the two institutions will be able to review and strengthen their partnership to provide more effectiveness in undertaking their challenging tasks.

Let me now touch on some features of Myanmar's economic development. Since the latter part of 1988, streamlining of foreign trade procedures and liberalization of both internal and external trade had been introduced. Foreign investors are allowed to invest in Myanmar and foreign bankers are permitted to open their representative offices. Myanmar has been participating in regional cooperation programs and cooperating with both developed and developing countries for its technological advancement. Rural and border areas' development activities are being implemented to alleviate poverty and also to reduce gaps in differences between rural and urban populations.

As over 60 percent of the population reside in the rural areas, the increase in farm income through the promoting of agricultural production has been the most appropriate strategy applied for poverty alleviation.

As agriculture is the mainstay of the national economy, 60 percent of the total population has been engaged in the agricultural sector, and it has been 35 percent of GDP, the promotion of agricultural production is fundamental for poverty reduction in both rural and urban areas. Efforts are being made to promote agricultural production with special emphasis to boost production of paddy, beans and pulses, sugarcane, and cotton, which have now been carried out through intensive and extensive cultivation with modern technical know-how.

With respect to the rural development programs, the policy objective of regional development in Myanmar is mainly toward self-sufficiency and self-reliance by promoting all-around development through exploration and effective utilization of natural resources of the region, by provisioning of the required inputs, and also by infrastructure development. To raise the living standard of national races who have remained underdeveloped and lagged behind for decades, and also to alleviate poverty in rural areas, the government has effectively and systematically carried out the development of the border areas and national races since 1989 through multifaceted programs.

Myanmar has made all-out efforts to promote economic and social progress without substantial external multilateral cooperation. A market-oriented economic system has been pursued for almost a decade; a strong economic growth has been registered throughout the years. This does not imply that Myanmar is not in need of multilateral assistance in striving toward economic and social development, but this is to say that Myanmar could have more significant impacts and achievements in its economy with all the external multilateral assistance complementary to its national endeavors.

We are combating unemployment, drug abuse, HIV/AIDS, environmental destruction, and social distress mostly on a self-reliance basis, and it is obvious that now is the time to have solutions to cope with the magnitude of the above mounting problems with international cooperation. Rekindling old ties with the Bank is by no means a new cooperation pact, but it is rather reviving the “good old spirit” of the partners in the development arena.

Myanmar is the land with rich natural resources to be tapped for development purposes. Unfortunately, multilateral financial assistance to Myanmar has been unfairly suspended since 1988. Myanmar has been a legitimate member of the Bank and the Fund since 1952. As a legitimate member, Myanmar is fully eligible for the Bank’s development assistance. However, the Bank has neglected Myanmar’s development efforts and it has failed to assist Myanmar for the past 11 years. However, we have cooperated with the Bank and the Fund and we have been servicing our outstanding payments to the Bank regularly, up to the end of 1997. In the absence of major multilateral and bilateral donors, Myanmar managed its development needs with its own financial resources. However, I wish to say that the scarcity of financial resources hampers the implementation of various development activities, which are beneficial not only for Myanmar, but also for the region as a whole.

In fact, the Bank's ultimate purpose is to assist its members in endeavoring for their development. Moreover, the Bretton Woods institutions themselves had established their objectives to assist member countries without any influence in their decisions by the political character of the member concerned, but only economic considerations. I would like to exhort the Bank to assist all member countries on an equal footing, without any political bias. And I would also like to urge the Bank to assist Myanmar with concrete and tangible support for its economic development based only on economic considerations.

Taking this opportunity, I would also like to mention that the Myanmar government has been striving for all-around development in political, economic, and social fields to pave the way for the emergence of a peaceful, tranquil, and new modern developed nation in accordance with the 12 objectives laid down by the state. Fulfillment of the need for food, clothing, and shelter is the most basic human right, and thus the government is fulfilling the people's requirements at its utmost by easing the food, clothing, and shelter needs of the people. The government has been making efforts to uplift the quality of the people's life and is also striving for the emergence and process of a proper democratic system. Myanmar really needs external financial cooperation at such a time of stringency, and it would greatly appreciate it if the Bank took positive initiatives toward a return to normalcy.

In conclusion, let me reemphasize the critical role the Bank and the Fund play in continuing their concerted efforts to develop the international monetary and financial system and in promoting the enhancement of the development process. I am confident that the Bretton Woods institutions should exert themselves to have the important tools to respond to their future challenges in the developing world with the most flexible initiatives in the area of cooperation among the developing and developed countries.

STATEMENT BY THE GOVERNOR OF THE BANK FOR NEPAL

Ram Sharan Mahat

It is a great honor and privilege for me to address the Annual Meetings of the World Bank and the International Monetary Fund. The role of the World Bank and the IMF was unprecedented this year because of the global financial crisis that started in East Asia last year. We have noted with interest that the Bank is moving beyond its traditional focus of funding individual projects to pumping fast-track rescue package loans—which was earlier considered to be the role of the IMF. This has also necessitated redefining and delineating the roles of the Bank and the Fund. We think it is an appropriate time that we revamp these institutions, thus giving them new vigor and strength to deal with changed circumstances. Given the linkages between macroeconomic and structural issues, there is a clear need to provide interrelated and properly sequenced assistance by the two organizations. In this regard, we welcome the proposed Bank-Fund initiatives to foster closer collaboration, which include the review of Bank-Fund collaboration in strengthening financial systems and the pilot program for enhanced Bank-Fund collaboration in low-income countries.

We thank the Bank for the progress made so far in the HIPC Initiative. We are confident that with the extension of the eligibility period of the Initiative for two more years, more countries will benefit from this initiative. We also support the assistance to post-conflict countries and urge other creditors and donors to complement the Bank in this endeavor.

It is commendable that the IMF has been active in raising financial resources to add to its fund. The increase in quotas of member countries also enables easy access to these funds during a time of need. We strongly urge all member countries to make appropriate arrangements so that the requirements for making the new quota system effective are met soon.

This year's Annual Meetings are being held at a time when the world is passing through a difficult period. The countries in the East Asian region have suffered severe economic setbacks. The economy of Japan is also under pressure. Transition economies, particularly the Russian Federation, are also in crisis, despite tremendous IMF financial backing and support from the world economy. Currency crisis, banking, and economic turmoil have become common phenomena in a number of countries. We firmly believe that the Bretton Woods institutions and the world community, together, will come out with a reform package to help overcome the problems on an urgent basis before the turmoil also spreads to other economies, leading to a situation of full-blown financial crisis. In the process of tackling the problems faced by countries in turmoil situations, the interest of smaller developing countries with a high degree of poverty should not be overlooked.

Time is a crucial input for development. Time needed for designing and processing a program and disbursing the fund should be carefully minimized. Likewise, recipient countries should devote greater attention to the effective implementation of the development program. I believe that the pace of development depends on these commitments.

Nepal embarked upon an economic reform program in 1991, which led to the series of reforms in trade, industry, tax, and foreign exchange regimes, in line with the imperatives of a liberal and open economy. The private sector was allowed to play a broader and dynamic role in the economy, and the government declared a policy of gradual disengagement from the management of public enterprises. In the six years since 1991, the economy was growing at a rate of 5 percent or more, with relative financial stability. The situation deteriorated last year. During FY 1997/98, the GDP is estimated to have grown by only 2.3 percent, the lowest growth rate since 1986/87. The agriculture growth rate was less than expected, and private sector investment did not pick up. Revenue growth was not as expected, and the development expenditure also slowed down. When the present government came into power in April 1998, the government took various measures to mobilize additional revenue, curtailed unproductive expenditures, and accelerated the privatization process. We have succeeded in regaining the confidence of the people. Now revenue has shown encouraging signs of growth, and investment has started to pick up. In order to strengthen domestic resource mobilization efforts, the government is committed to implementing the value-added tax effectively.

Attainment of economic efficiency through the privatization process has been given priority. In this context, in the past six years the government has privatized 16 public enterprises, and 4 major public sector undertakings are currently in various stages of privatization.

A sound financial system is a prerequisite for the smooth functioning of the national economy. Our commitment has, therefore, been to augment financial sector reform so as to create a conducive atmosphere for healthy and sustainable economic development.

Equally important challenges for the Nepalese economy are to achieve broad-based growth and address the issue of poverty. These are challenging and complex issues. We believe that the development activities should be initiated at the grassroots level with the meaningful participation of the stakeholders. People should be in the forefront of the development process and they should take a lead role in ensuring the investment efficiency and sustainability of the project benefits. In order to reinforce the participation process, the parliament has recently passed a Local Governance Bill, which will give more authority to the locally elected bodies in terms of revenue mobilization, allocation of resources, and implementation of development activities.

Infrastructure development is crucial to Nepal's economic development. Establishment of a rural road network, harnessing of water resources for irrigation and power development for domestic as well as the export market, and expansion of the rural telecommunications are some of the prerequisites to reduce rural poverty, and the development of these sectors calls for higher investment. We have consistently increased the allocation for the social sector. In the current year's budget, more than one-third of the development budget has been allocated for the social sector. Here again, in order to improve the quality of services to the rural areas, expansion of the rural infrastructure network is essential. This is also a prerequisite to enhancing the capacity of the economy to accelerate the growth rate. We therefore urge the international community to support the development of Nepal's poor infrastructure sector, without which the goal of reducing poverty will become a distant dream.

The revised document of the Ninth Plan (1998–2003) has outlined a perspective for Nepal's long-term economic development. This plan at its core has set poverty alleviation as its sole objective, aiming to reduce the population under the poverty line by one-fourth. The targeted GDP growth rate is 6.0 percent annually. The plan also seeks to limit the growth of the money supply at 13 percent, while anticipating inflation at 6.5 percent. In order to achieve the targets, the plan has envisaged, within the framework of the goals defined by the Agriculture Perspective Plan, rural development with a greater focus on social services, agriculture growth, and income-generating activities, and the development of infrastructure, including the construction of rural roads. It will ensure the involvement of the civil society in socioeconomic development. The government will play the role of the facilitator. The promotion of the private sector, especially in industrial, trade, tourism, and other service sectors, is the core of the reform program.

The government is committed to providing good governance and addressing the problem of corruption. Corruption is a complex issue with social, political, legal, and institutional dimensions. It requires the efforts of both the donor and recipient communities to fight this menace. We therefore seek the World Bank's cooperation in tackling this problem.

We firmly believe that the international community will support our efforts by providing an increased level of concessional finance, particularly to the poorer countries. We are encouraged by the recent announcement by the U.K. government that it will increase its development assistance by 25 percent. We expect that IDA-12 negotiations will be successfully concluded by the end of 1998 to avoid any uncertainties. Judicious and efficient utilization of increased development assistance will not only help to avert the problems that many countries are faced with, but also make the world a better place in which to live for millions of people who have never had a chance to acquire even the basic needs of life.

Statement by the Governor of the Bank for the Netherlands

Gerrit Zalm

The Policy Response of IMF and World Bank

As we all know, the world economy is currently experiencing serious financial instability. In this difficult situation, the IMF's response has generally been adequate and continues to be supported by the Netherlands. Also, we support the Bank's efforts to assist countries in implementing the necessary structural reforms in the financial and the corporate sector and to alleviate the effects of the crisis on the poorest and most vulnerable. In a number of Asian countries, recovery is now under way. However, in other cases, efforts to restore confidence have not yet brought about the desired result. This warrants a careful evaluation of the policies of the countries concerned and of the response of the international community. In this respect, both sufficient availability of funding and appropriate burden sharing between public and private actors are essential.

Financial Sector Management

In the meantime, it is possible to formulate a number of preliminary lessons to be learned from the crisis and the international response to it. A core lesson for IMF and Bank members is that sound macroeconomic monetary and budgetary policy are a necessary, but not sufficient, condition for financial stability. A healthy financial sector safeguarded by adequate and effective supervision is similarly important. We welcome the initiatives that have been taken in response to the Asian financial crisis by the Bretton Woods institutions and by other international organizations to enhance and monitor standards in financial sector supervision. Further technical assistance by the international community to help emerging markets in establishing sound financial sectors is urgently needed. For this, we do not need to create a new international organization. That would only divert attention from the urgent real issues. We have already assigned to the IMF the task of monitoring the implementation and observance of the Basle Core Principles. This monitoring should preferably form a regular element in Article IV consultations. In our view, Fund resources should be redirected to this end. In addition, the World Bank should further increase its capacity to assist countries, also proactively, in strengthening their financial sectors. I do think that these efforts need to be further stepped up and coordinated where necessary.

Hedge Funds

Particularly in periods of financial distress, sizable bank losses resulting from excessive risk taking may lead to a rapid loss of confidence in financial markets, seriously increasing systemic risk. In recent weeks, we have seen the near collapse of a hedge fund. The lessons to be drawn from this event are twofold. First, transparency of hedge funds should be improved, so that all parties associated with hedge funds are aware of the risks they run. Second, the sheer size of banks' exposure to these funds is worrying. In our view, the Basle Committee should take the lead in examining these issues further.

Capital Controls

A number of emerging markets have responded to the financial instability by unilaterally introducing controls on capital outflows. Indeed, the destructive forces of large-scale inflows followed by massive outflows has given rise to a debate about the desirability of international capital mobility. It also delayed progress on a proposed amendment of the Fund's Articles of Agreement to extend the Fund's mandate to overseeing the orderly liberalization of international capital flows. However, we should not lose sight of the fact that the free flow of international capital has made a significant contribution to economic development over the past decades. The recent crisis has made clear once more that, in liberalizing capital flows, appropriate sequencing is crucial. Liberalization should start by opening up an emerging market for foreign direct investment; more volatile flows of capital can be liberalized only after a stable financial sector, with adequate supervision, has been established. As a transitory measure, market-oriented controls on short-term inflows, as successfully implemented in some emerging economies, can be helpful in securing that foreign capital is used for productive investment and genuine trade financing. The final objective should not be to abandon international capital mobility, but rather to create a stable and transparent framework for international capital flows, in terms of both sound macroeconomic fundamentals and sound financial sector supervision. We expect the Fund to continue to take the lead in the current debate.

It is important to note that restrictions on short-term capital flows cannot be a long-term substitute for sound macroeconomic and regulatory policies. In those extreme cases where temporary restrictions could help to create breathing space to implement the necessary adjustments, they should be applied in the context of an IMF-supported adjustment program.

Burden Sharing Public-Private Sector

Another core lesson to be learned is that the sums involved in IMF-led rescue programs are nearing a level that is undesirable in view of the moral hazard implications for the private sector. In a global economy with huge and ever-increasing private capital flows, public money simply cannot provide a full rescue whenever private creditors panic en masse. Large-scale efforts may seem an energetic response to crises and hence carry some public appeal, but they raise unwarranted expectations. It is of paramount importance that private investors be involved in rescue operations at an earlier stage. The importance of private sector involvement is reinforced by the difficulty of activating second lines of defense in bringing about financial support.

In my opinion, the Fund should play a more active intermediary role in bringing about a contribution by private creditors, and Fund support should be made conditional on their contributions. Efforts should be made to establish more structural contact with creditor groups, such as the Institute of International Finance.

Rethinking the Architecture of the International Monetary System

We strongly believe that the IMF is the proper place to decide on the future of the international monetary system. The key is to strengthen its capability to prevent and withstand financial instability. Our Interim Committee should remain the core forum for these discussions. If the present arrangements for its meetings do not cater enough to having effective discussions, we should focus on creating the opportunity for that.

Fund-Bank Collaboration

In responding to the international financial crisis, we should ensure that Fund and Bank do not duplicate, but remain complementary. They should continue to focus on their primary responsibilities. The Fund should continue to be focused on macroeconomic stability and restoring confidence in times of crisis. Medium- and long-term structural policies are primarily the responsibility of the Bank. In this respect, we welcome the attention paid by the Bank to the social consequences of crises. In cases of overlap such as the efforts to strengthen the financial sector in emerging markets, the need for good cooperation is evident. We welcome the improved Bank-Fund cooperation in specific pilot cases as a follow-up to the ESAF evaluation. The Bank should not engage in large-scale balance of payments financing for the crisis countries, an activity for which it lacks the mandate and the instruments.

IBRD Net Income

Apart from the mandate issue, the provision of large-scale balance of payments support puts undue pressure on the financial capacity of the Bank and shifts that burden onto the borrowers. A more equitable burden sharing could very well involve a capital increase. Declining net income cannot adequately provide sufficient funding for reserves and for the other purposes that shareholders want the Bank to finance. We must be aware that there is a limit to what we can ask the Bank to do. We would therefore urge shareholders to live up to their responsibilities and contribute adequately to the HIPC Initiative and IDA.

The international financial institutions cannot continue to respond to international crises by supplying ever larger rescue packages. All actors, including the countries concerned and the private sector, should strengthen their efforts to avoid further turmoil. The Fund and the Bank should be provided with the necessary means to continue to play their roles. In this context, I am glad to be able to announce today that the IMF quota increase has been approved by the Dutch parliament.

Statement by the Governor of the Fund for New Zealand

W.F. Birch

This Annual Meeting of the IMF is pivotal to economic confidence and a recovery of growth in the world economy. We can continue to endorse open market fundamentals, and lead the world—including developing, emerging, and transition economies—into a new era of global growth. Or we can encourage nations into the blind alley of renewed protectionism and other inward-looking policies, setting back for many years the achievement of that growth.

I welcome the focus now being developed by the G-7. The contribution of the large industrial economies to confidence is crucial. But smaller economies have a role to play too, if they run open stable policies that maintain investor confidence.

There will always be cause for concern about the volatility of capital flows where countries have not yet set in place the fundamentals of a sound economic framework—where financial sector reform has not been addressed, bad loans abound—where governance and bankruptcy arrangements are inadequate. But where capital is desperately needed to lift the living standards of a people, it is no answer to shut out that capital or impose constraints that boost its price. The message of this conference has to be that the best protection against volatility is always to establish, at the domestic and international levels, a sound economic and fiscal framework.

In my country, New Zealand, in the 1970s and early 1980s, we had had one of the most protected economies in the western world. Designed to protect, it greatly increased our vulnerability. We went through, in the mid-1980s, the same process of rising debt, exchange rate crisis, capital surges, inflation, and banking problems seen more recently in Asia. Without reform, the impact of the Asian crisis on New Zealand would inevitably have been high interest rates, serious bankruptcy, and massive unemployment. Instead, in 1985, we floated the kiwi dollar. It is universally understood today that the government and central bank are not going to prop it up. This is a totally clean float. Banks and corporates know they have nothing to gain from undertaking unhedged foreign exchange liabilities. The exchange rate adjusts freely, in line with economic fundamentals.

We base our policy framework on five principles:

- an open economy, open trade policies, and open capital markets;
- price stability as the sole statutory priority of the central bank;
- prudent fiscal policy, including a buffer against fiscal shock;
- flexible labor markets; and
- a low-rate broad-based tax system.

Those policies have trebled our growth, halved net public debt, cut net public foreign currency debt to zero, cut unemployment from 11 percent to 6 percent, and transformed our economic future.

If we want exporters to compete globally, we have to give them world input prices. Legislation passed last week timetables the removal of all remaining tariffs by July 2006. New Zealand has increased its Asian exports by 75 percent since 1990. Last year 7.8 percent of GDP and 36 percent of total exports went to Asia. We have more exposure to Asian markets than any other Organization for Economic Cooperation and Development (OECD) nation, leaving aside Japan, Korea, and Australia, so inevitably, the Asian crisis hurt us. We expect –0.5 percent growth in the year to March 1999. Fiscal surpluses are off the table for two years. But we see growth recovering late this year to 3 percent in 1999–2000, and 4 percent in 2000–01.

New Zealanders exporting into a flat Japanese market have been able to boost sales by 20 percent in recent years. Large competitive efficiency gains in the past three to four years now combine with a major movement of the kiwi dollar in their favor. Even on the low-growth assumption that demand for New Zealand exports goes on contracting till late 1999, our Treasury expects growth to average above 2.8 percent in 1993–2001.

There are, however, clear risks to global growth in the period ahead. In this environment, the IMF has a key role. Accountability is fundamental. If banks can make bad lending decisions with relative impunity from financial consequences, there will be no end to bad loans they make. The IMF has to be more than a financial bank. It should also be a knowledge bank—a provider of surveillance, expert advice, and even more important, an assurance of transparency. Transparency is central to responsible management. It is not, as somebody here described it, “motherhood and apple pie.” For the banking sector, in particular, it is the critical discipline.

Like central banks at the national level, international financial institutions have, at the international level, a responsibility to warn where imprudent activity is creating risks for financial or economic stability. They did not, in the run-up to the Asian crisis, warn adequately of the underlying risks to stability. True, others also missed the boat. But the international financial institutions have a special responsibility. This Annual Meeting is pivotal, in particular because the juggernaut set in motion by the Asian crisis may have some distance yet to travel, before we can halt its destruction.

I am encouraged by the steps already taken by Asian countries such as Korea and Thailand, but big risks still remain for the world economy. It may be, for example, that growth in the U.S. economy in 1999, reduced by events elsewhere, may fall as low as 0–1 percent. That would cause impacts in Europe and worldwide. If so, it would be difficult in the extreme for nations to find their way through that minefield, without clear, strong delineation from the IMF and World Bank of the best choices to make. Confidence depends on being able to identify a reliable path through all these present difficulties into a better global future. Without leadership, the risk of a return to ad hoc protectionism based on myopic analysis and self-defeating policies is enlarged to seriously dangerous proportions. Providing that leadership and confidence is, in my view, the key task of this meeting.

Statement by the Governor of the Bank for Pakistan

Hafiz A. Pasha

It is my privilege to participate in the 1998 Annual Meetings, to which I welcome the Republic of Palau as a new member, and also record my appreciation of the Joint Secretariat for the excellent arrangements made for these meetings.

This year’s meeting is like no previous meetings. At no time in the past has the role of two institutions, the IMF and World Bank, been as seriously questioned as is being done today. Hardly a day goes by nowadays without the appearance of a leading article in the most influential newspapers and journals, written by some of the most eminent academics, political leaders, and persuasive authors of the world, on the role of the IMF and the World Bank. To be sure, there has always been some confusion over the respective roles of the IMF and the World Bank. Remember that Lord John Maynard Keynes, more a founder of the two institutions than anyone else, was perplexed at the inaugural meeting of the IMF. He thought the Fund should have been called a bank, and the Bank should have been called a fund.

Clearly, we are at the same crossroads that we were in 1944 at Bretton Woods. The present crisis has brought home to us, in stark terms, that, while global economic integration has presented developing countries with new opportunity, it has also has incurred huge costs. Policymakers now have to contend with far too many exogenous factors. For instance, the world economic outlook, as outlined in the October 3 communiqué, alludes to a substantial fall in commodity prices, which is adding to the difficulties of many countries and to deflationary pressures on the global economy, as a result of which developing countries have suffered losses in export opportunities, income, and production. To these are added the social and economic costs of adjustment. The additional risk of destabilization imposed by unbridled capital movements is grounds for intense anxiety, which has already gripped these meetings.

We in Pakistan have often pointed out the dangers inherent in too rapidly liberalizing capital movements in economies in which the macroeconomic framework and the financial sector are weak. Liberalization must be phased not only in accordance with the external situation, but also with regard to the country's internal situation, and the depth and breadth of its markets and institutions. Without prior financial sector reforms, there may be distortions in the regulatory structures that might accelerate capital movements unrelated to the underlying economic situation. Based on these considerations, we have always argued for an appropriately sequenced adjustment strategy. Much of our discussions with the Fund have centered on the sequencing and ownership of reforms, which are the cardinal guiding principles.

This brings me to the important point about ownership of reform programs. Ownership cannot be externally induced or imposed. I am not rehearsing here the familiar condemnation of "conditionalities." That would only be political rhetoric. My point is a more substantial one, that in its doctrinaire adherence to standardized economic prescriptions (the officially sanctified remedy for all ills), the IMF at times ignores homegrown measures that can be more effective than those that are externally imposed. The unfortunate consequence of these attempts at adherence to a uniform economic theology is that hardly any attention is given to the context of a program. The great virtue of an indigenous reform effort is disregarded. Small wonder that IMF programs run into questions of ownership and arguments over the sequencing and timing of administering therapeutic treatment.

My fellow Governors, we in Pakistan have always been great supporters of the Bretton Woods institutions and will continue to be in future. We have continually argued for greater and sustained replenishment of the IDA. We also favor a capital increase, which is the only long-term solution for ensuring that the Bank can provide financing for projects that the G-7 is itself encouraging the Bank to assist in. We also support the further replenishment of IMF quotas.

Elimination of poverty was the prime purpose of the Bank and the raison d'etre of IDA. Despite a half-century of effort, poverty remains the biggest curse of mankind. One can even argue that some of the indices of impoverishment have, in fact, worsened. However, with the arrival of Mr. Wolfensohn, there has been a renewed vigor to get back to the Bank's first principles. We, in the third world, are deeply appreciative of his vision of the "strategic compact" and realignment of priorities for removal of hunger, want, malnutrition, and disease. The five-point conceptual framework that he unfolded yesterday could not have come at a more opportune time. We assure the management of both institutions that we are solidly behind them as they trace their steps along the "markers" that the Chairman has so eloquently talked about.

Finally, let me give you a brief report on the economic situation in Pakistan. Pakistan had undertaken a bold structural reform program in February 1997 when our government assumed office. The economy was beginning to respond positively to the program with an increase in growth from 1.3 percent in 1996–97 to 5.4 percent in 1997–98, a reduction in the fiscal deficit to a five-year low of 5.4 percent of GDP and a lowering of the rate of inflation, to 7.8 percent from a double-digit level in the preceding years. Pakistan was therefore able to meet all the performance criteria under the ESAF and extended arrangements with the Fund. Despite this commendable performance, our program received a severe setback, as our response to our regional security problems triggered sanctions against us. The sanctions also affected our relationship with the international financial institutions. Even the Fund-supported program was put in abeyance despite Pakistan having met the performance criteria. This disruption in our normal financing has led to severe difficulties, requiring emergency measures. We are doing all that we can to continue with our reform program and are in the process of negotiations with the IMF. I am confident that the world community will be willing to support Pakistan in this endeavor.

Statement by the Governor of the Bank for Papua New Guinea

Iairo Lasaro

I would like to take this opportunity to welcome Palau as the new member of the World Bank and the IMF, and as a member of the Pacific

Group. I would also like to join the previous speakers in sharing our experience in coping with the current economic and financial difficulties affecting many parts of the world, and indeed the smaller nations in the South Pacific region. This meeting is timely, as it allows us to address common issues together, learn from each other, and look for options and solutions to assist in minimizing the impact of these difficulties.

The current problems in Russia add to the world's economic difficulties. I know this is being closely monitored by international financial institutions and agencies in various fora—most recently in Ottawa, Canada, last week at the Commonwealth Finance Ministers' meeting. At this juncture let me express my appreciation to the World Bank and the International Monetary Fund for providing assistance to the member countries affected by this crisis. Although this has provided some relief to the economies affected, the problems appear to have penetrated the basic structure of their economies, thus affecting the general economic activity of these countries, their trading partners, and other countries in the region. We are likely to see a worsening situation and, therefore, we should seriously look at establishing some form of international relief, while not ruling out an improvement to the outlook of the East Asian economy and the world economy. While the financial aspect of the crisis is being dealt with, we need to reinforce the international efforts to address the social dimensions of this unprecedented crisis, which has pushed millions of people below the poverty line in the affected countries. In this context, I propose to the Fund and to the Bank to consider the idea of debt relief for poor countries as currently extended under the Commonwealth umbrella.

Allow me now to outline the developments in Papua New Guinea over the past 12 months.

Recent Economic Developments

I wish to place on record our government's appreciation for the assistance provided to Papua New Guinea by the Fund and the Bank, particularly in recent years. In late 1994, the Papua New Guinea economy experienced a balance of payments crisis, resulting from expansionary fiscal policy in the early 1990s. The crisis prompted a marked change in fiscal, monetary, and exchange rate policies. Strict expenditure controls were introduced to bring the fiscal deficit under control, monetary policy was tightened substantially, and a floating exchange rate regime was introduced.

In early 1995, the government introduced a macroeconomic stabilization and structural adjustment program, which was supported by a World Bank Economic Recovery Program loan and a Fund Stand-By Arrangement. Among other areas, the government program focused on the reestablishment of macroeconomic stability. The government's program produced positive results. The economy stabilized and economic growth resumed. During

1995, fiscal policy was tightened to allow a budget deficit of ½ of 1 percent of GDP for the year. In 1996 the deficit was brought into surplus of ½ of 1 percent and again in 1997 a small budget surplus was achieved. Concurrent with improved fiscal management was a turnaround in the external accounts. In both 1995 and 1996 balance of payments surpluses were recorded. These surpluses were underpinned by very healthy performance in the current account, particularly in a positive merchandise trade balance.

Economic growth resumed in late 1995, and throughout 1996 the economy expanded strongly. This growth continued in early 1997. All of these goals were achieved against the backdrop of favorable external factors, including strong economic growth in Papua New Guinea's export markets and relatively good mineral and commodity prices.

The year 1997 was embarked upon with much the same favorable external environment, and until mid-1997 the Papua New Guinea economy performed well, registering strong current account surplus and strong activity in the nonmining private sector.

In mid-1997 Papua New Guinea faced its worst drought in living memory caused by the El Niño weather phenomenon, which affected seriously the rural economy and the livelihood of more than 1 million people. The situation turned into one requiring a large-scale humanitarian supply of staple food items and water to rural communities. A quick response avoided many deaths caused by starvation and subsequent epidemics of disease. The economic impact of the worst drought in Papua New Guinea's history was reflected in a drastic shortfall in export revenues and a sharp general economic contraction. This was prompted by sharp falls in agricultural production in some areas and temporary closure of two of the country's largest mining projects as rivers dried up.

While the drought has subsided significantly, some sectors of the Papua New Guinea economy are yet to fully recover. As if the drought was not enough challenge for our government—which was elected into office in July 1997–-in late 1997, Papua New Guinea faced a formidable challenge posed by sharply falling commodity prices, which were the result of the East Asian financial crisis. This involved very large falls in oil, gold, copper, and log prices. The substantial declines in both prices for and volumes of these exports in 1997 left Papua New Guinea with a large balance of payments deficit by the year's end.

As in the case of several other countries in the region, the balance of payments crisis put significant pressures on our currency beginning in mid-1997, but particularly in the first half of 1998, resulting in a 40 percent depreciation of the kina. In response, in July 1998, our government introduced several bold measures to reinforce fiscal and monetary controls which had been built into the 1998 budget, in order to arrest further decline in the exchange rate. Stability of the exchange rate has been achieved since late July, with the kina remaining within a band of 40–45 U.S. cents.

The Governors will also recall that Papua New Guinea has continued to suffer from the ravages of nature in 1998. The tidal wave disaster that struck Ataipe in the West Sepik Province of Papua New Guinea further increased pressures on the government's budget. Furthermore, sustaining the encouraging peace initiatives on Bougainville Island has required substantial expenditures on rehabilitation and peace accords. Maximizing the probability of peace will necessitate increased funding to the province to restore the social and economic infrastructure.

In line with the mandate of our people, our new government has initiated, and made significant progress in putting in place, the necessary legal framework to combat widespread corruption in the public sector, and to improve public service delivery. A draft bill to establish an Independent Commission Against Corruption is before the parliament, and the government is committed to a bipartisan support to make the act effective.

Our government has also taken major steps in unleashing the economic potential of Papua New Guinea. A major reform of the tariff and excise tax system has been passed by parliament to become effective on January 1, 1999. A second piece of value-added tax legislation has been considered by the parliament and awaits its third and final reading before the end of this year. These are major achievements by any standard and are fully in line with the international trends in integrating Papua New Guinea into the global economy.

The Papua New Guinea government is determined to further encourage and promote fair and equitable development as enshrined in the constitution, by maintaining a stable macroeconomic environment and law and order. This commitment has been demonstrated repeatedly, most recently by Prime Minister Bill Skate's visit to the IMF and the World Bank. In addition to implementing policies designed to restore economic stability, our government has pursued policy dialogue with both the IMF and the World Bank with a view to obtaining a Stand-By Arrangement, together with a Social and Economic Development Program loan. However, for the past two years, Papua New Guinea has been forced to go through a recovery path alone while many other countries with access to substantial private capital inflows have succeeded in receiving significant support from the Bretton Woods institutions. Furthermore my government is confident we will emerge from the current "challenging period" with economic stability intact and an economic structure from which social development can rapidly progress.

Papua New Guinea calls on the World Bank and the International Monetary Fund to not limit their focus to addressing the problems of only the larger economies. The challenges faced by the smaller nations in the region are as real as those of larger countries. However, with the limited access of smaller and emerging economies in the Pacific to other sources of funding, the IMF and World Bank's failure to assist them could indeed result in unspoken social devastation and poverty.

STATEMENT BY THE GOVERNOR OF THE BANK FOR PARAGUAY

Heinz Gerhard Doll

It is a privilege for me to address the participants in these Annual Meetings and to convey greetings from the people and new government of Paraguay. We would also like to join in welcoming the Republic of Palau.

My country has not been spared the effects of the global economic events of recent years. This has required a major effort to adopt domestic policies in a timely manner, so as to minimize the adverse impact on our economies while enabling us to find prompt responses to the nation's social problems.

The challenges involved in grappling with the recent financial crises, whose effects are spreading to the rest of the world, have had a major impact on the development of the smaller economies, which have had to make greater efforts to overcome their domestic problems as well. That is why it is important for these issues to be discussed at the Annual Meetings with all member countries of the World Bank and IMF, in order to identify appropriate and timely solutions for the emerging economies, which are having to cope with the fallout from events unfolding elsewhere. Accordingly, the core objective of Paraguay's new government, which took office on August 15, has been to achieve sustainable economic growth through development of the production base, grounded in competitiveness, as a means of ensuring social development for the people. The government's strategy is therefore aimed at strengthening the macroeconomic environment based on a market economy and greater involvement of the private sector, considering that the government's efforts will focus on promoting the rationalization and reorientation of public expenditure.

With this in mind, we have decided to embrace the economic, social, and political challenges of improving our nation's fortunes by consolidating the reforms of our financial sector, deepening state reform, enhancing the transparency of government management, boosting productivity, and raising quality standards, with the aim of increasing national savings and exploiting the potential advantages that the Southern Cone Common Market (MERCOSUR) offers. Furthermore, our goal is to improve public services, broaden the coverage of social services, and ensure equal opportunities for the entire population, so as to embark on a course of sustained and sustainable development.

As part of this strategy, from the outset we adopted a policy of austerity in fiscal expenditure and, in the first 45 days of our administration, we reduced government outlays by 11 percent relative to the same period of 1997, while prioritizing education, health, infrastructure, and basic services. With the aim of enhancing our performance in the area of tax collection, we are upgrading our tax supervision and audit mechanisms with a view to boosting tax revenue. In the early days of our administration, we successfully increased the tax yield by 10 percent in relation to the same period of 1997, notwithstanding a sizable reduction in import volumes. The most important measures include the consolidation of education reform as the principal tool of development and poverty reduction. In addition, we have established a program of disease prevention and health promotion for the most vulnerable segments of society, focusing on high-risk, low-income groups. To achieve the objectives which I have described, the current national government is awaiting parliamentary approval of a substantial package of economic, social, and social security laws.

We have already enacted laws to prevent and punish unlawful acts associated with money or asset laundering, as well as trademark law, copyright, and safeguarding individual property rights. We have also introduced laws aimed at the promotion and reciprocal protection of investment, a law to govern the securities market, and the external audit law, in the interest of facilitating capital market efficiency and capital investment. The national government is cracking down on money piracy and money laundering activities. The success of this policy is evidenced by the fact that 32.6 percent of all the assets seized between 1993 and August 15, 1998 can be attributed to the current administration.

With respect to modernization of the state, the national government is seeking to encourage capital investment in public enterprises by the private sector, with the aim of eliminating market distortions, increasing the production and supply of goods and services in an environment of competitiveness and efficiency. In this context, the parliament is considering laws on the capitalization of the telecommunications enterprise and the regulatory framework governing the supply of drinking water and environmental sanitation. The parliament will shortly be examining the regulatory framework governing the generation, transmission, and distribution of electric power. Also, the public sector banking reform will be deepened for the purpose of providing agents of production with efficient technical and financial assistance, by ensuring that financial resources can be appropriately channeled through loan portfolios for the agricultural, industrial, and housing sectors.

Furthermore, we are encouraged by the efforts to review the principles of cooperation and collaboration between the World Bank and IMF, as a way to ensure coordinated and expeditious operations by both institutions in the socioeconomic and structural reform areas. Such action should make it possible to improve the supervision process and its results, facilitating an appropriate choice of priorities in lending programs, and enhancing the capacity to respond to the future crises that are liable to continue affecting the global economy. In closing, we anticipate that these Annual Meetings will be successful in enhancing and improving the design, implementation, and evaluation of future socioeconomic policies.

STATEMENT BY THE GOVERNOR OF THE BANK FOR THE PHILIPPINES

Edgardo B. Espiritu

The joint meetings of the International Monetary Fund and the World Bank are taking place this year amid one of the most severe tests to world economic stability in the past two decades. Not since the severe economic contractions of the early 1980s, triggered by the large debt overhang of many developing countries and the weakening of the financial systems of creditor countries then, have we seen a crisis as pervasive as the present one. Not even the Mexican crisis in the early part of this decade can compare with it.

Indeed, some even go so far as to say that today the world economy is under the worst threat that it has experienced in the post-World War II era. According to them, if ever there was a crucial test for the Bretton Woods institutions' ability to fulfill their missions of guarding the stability of the world financial system and bringing about sustained economic development, this is it.

The fact that the present crisis began in the emerging economies of East and Southeast Asia, which have long been considered the bastion of the idea that free markets are the best way of bringing about continued economic prosperity, makes it all the more significant. It seems that it was just at the very high point of the world's faith in the market, even among those countries that used to be under so-called command economic systems, that suddenly this turmoil erupts. Thus, many now again doubt the ability of the market to achieve the desired results. In fact, some countries have begun or are considering moving away from free market principles. This, to our mind, is rather unfortunate. The market has served the emerging economies of Asia and of other regions well. Moreover, most of those who have studied the causes of the Asian crisis have come to the conclusion that among these causes is the fact that there were distortions and structural deficiencies in the crisis countries that prevented markets from working well. One should not therefore be too hasty in discarding free-market-based economic policies.

Yes, the players in the market should not be left to their own designs. But governments should resist any temptation to again put free markets in fetters and to abandon liberalization altogether. Governments, though, will have to redefine their role in the economy as well as the idea of liberalization. Essentially, I believe government's crucial role is to provide a clear, transparent, and evenly applied regulatory framework. Government should not compete with the private sector nor arbitrarily intervene in its economic decisions, but it should likewise ensure that the institutions and mechanisms required to effectively oversee economic activities, particularly those of the financial and corporate sectors, are present.

Without going into any further discussion of the swings in sentiment throughout history between the relative merits of the market and of the state in organizing economic activity, let me just observe at this point that at least two of the economies originally hit by the crisis are now on their way to recovery after painful but still market-oriented measures. But new threats now loom on the horizon. The troubled emerging economies have relinquished center stage to the giant economies in the region. It is what happens to the currencies and economies of these big players and the contagion effects on other economies, that reach as far as Latin America, that now threatens world economic stability. It is now feared that if the disease in Asia worsens, the outbreak will reach the industrialized countries themselves.

The joint meeting this year therefore cannot but include in the agenda the question of how to prevent another global depression. Even with the continued robust performance being exhibited by the world's biggest economy, the United States, still we cannot ignore this threat. The suddenness and the unexpected gravity of the Asian crisis should have taught us this.

The character of the world economy is vastly different and more complex than that prevailing, say, in the 1930s, or even in the early 1980s. The high level of global integration and capital mobility that now prevails has made uncertain whether solutions that worked before would still work today. However, we are still optimistic that on balance, the accumulated knowledge and experience on the workings of the world economy, the flexibility and adaptability of the countries and institutions involved, and the greater avenues for cooperation available today will enable us to avert another global recession.

We in Southeast Asia, together with certain other countries in the Asia-Pacific region, have realized earlier on the great need for cooperation in meeting this crisis and have come up with the so-called Manila Framework for this purpose. This framework provides for, among others, the establishment of a regional surveillance mechanism to complement the global surveillance being done by the IMF; for enhanced economic and technical cooperation, particularly in strengthening the financial systems of the countries in the region; and for a possible cooperative financing arrangement to supplement IMF resources.

I wish to reiterate my country's support and endorsement of this framework. While recognizing the central role of the IMF in keeping global financial and economic stability, we believe that a specifically region-based and quick-responding surveillance and cooperative action mechanism would help the Fund a lot in achieving this objective. We are happy to report at this point that there has been substantial progress toward establishing such a mechanism. The Association of Southeast Asian Nations (ASEAN) senior finance officials who have been tasked with carrying out the intent of the Manila Framework have, in their meeting in Kuala Lumpur last month, laid the groundwork for the setting up of an ASEAN

Surveillance Technical Support Unit. This unit, which will be based in Manila for two years and which will be assisted by the Asian Development Bank, will provide technical and capacity-building assistance to ASEAN governments toward putting the surveillance mechanism into operation. Hopefully, through this mechanism we shall be able to detect early enough any incipient problem or vulnerabilities in the region's economies and to take prompt cooperative action to remedy or contain them.

It is also very encouraging to hear the recent announcement from Japan's finance minister, Mr. Kiichi Miyazawa, of a Japanese assistance package for the crisis economies. This gives us renewed confidence that an important neighbor in the region is serious in its intention to take on a leading role in efforts to address the crisis.

We wish to note at this point that both the Fund and the Bank have, by and large, responded quite well to the Asian crisis, showing significant flexibility and adaptability in the process. More important than the foreign exchange funds that they provided to ease the immediate liquidity problems in the affected countries as a result of the drying up of capital flows, they helped these countries to pursue reforms that address their points of vulnerability. The solutions and approaches are still evolving, in many cases with important inputs from the assisted countries themselves. The Fund has often been criticized for allegedly failing to find effective ways to lick the crisis. But the question may be asked, what would have happened, what further devastation would have taken place, had the countries concerned not carried out IMF stabilization programs and complementary World Bank safety net and structural reform programs.

I say that instead of becoming irrelevant, these institutions have become all the more important in facing not only today's immediate financial turbulence but also the other potential problems that could emanate from major global trends. It is true that there may be a need for a rethinking of these institutions' roles, their internal structures and dynamics, as well as their approaches to the problems of their member countries, but the general direction should be toward strengthening rather than discarding them. We, therefore, view with a bit of concern what seems to be a lingering hesitation on the part of the Fund's biggest member countries to give it their full support by way of enhancing the Fund's capital base. We were, however, heartened to hear the statements made by President Clinton in his address at the opening of the joint meeting that the United States intends to keep its commitments to the Fund and that the G-7 countries are now urgently working on a program that will strongly address the crisis.

With regard to the World Bank, there is apparently a need to address its own long-term viability problems to enable it to carry on with its important mission of fostering sustained economic development of its member countries. The present concern is how to check the declining trend in the Bank's net income while at the same time maintaining adequate reserves and meeting countries' demands for assistance at these difficult times.

We note with concern, however, that most of the measures that have been suggested to address this problem put the burden almost entirely only on one group of countries, namely, the borrowers. The Bank, it is true, has in the last two decades been facing new challenges and has had to attend to new kinds of clients with varying needs. These include the heavily indebted poor countries, the post-conflict countries, and now the emerging economies that have been hit hard by the crisis and its contagion effects. Whether it is appropriate to have a multilateral lending institution like the Bank shoulder the bulk of the responsibility of providing assistance to certain countries that have special links with potential bilateral donor countries is one issue. But the more relevant issue now is the appropriate and equitable sharing of the burden of maintaining the Bank's financial viability. Just raising its lending rates, particularly on traditional facilities that cater to countries that have limited access to commercial funding sources, would indeed prove to be counterproductive and certainly unfair to these countries. As it is to all countries' interest to see that the Bank is in a position to facilitate the return and maintenance of global economic growth, all member countries should therefore share in the costs of buttressing the Bank's resources. We therefore believe that a general capital increase is the most equitable way of maintaining the Bank's financial integrity while allowing it to continue to effectively fulfill its development mandate.

The return of global economic stability and growth should indeed be the concern of all countries as well as of the multilateral financing and development institutions. Everyone needs the help of everyone else. But individual countries have the responsibility of seeing to it that their respective houses are in order. In the Philippines, we are continuing to pursue painful reforms in spite of the current difficult environment. We are continuing with the liberalization of important sectors. We have made a conscious decision of maintaining our integration with the global economy regardless of the present crisis. We are resisting any temptation to reverse this sound long-term strategy in exchange for any momentary gain.

When we survey the world economy at this time when the century is about to close, we can recognize the tremendous changes that have taken place. The experience of the newly industrializing countries and the emerging economies has raised hopes that a broader range of countries can achieve sustained economic progress. But recent events have again dashed these hopes. In their place, the specter of a possible world depression is again visiting us.

But if we keep our wits about us, we will realize that we are now better armed in facing this threat. Among the advantages we now have compared to two or three generations ago is the fact that international organizations now exist that provide the vehicle for coordinated and cooperative action. The Bank and the Fund, which themselves are institutions born of earlier crises, are still around. They have many years of accumulated experience and knowledge, which although may still be in a state of flux in relation with the present crisis, are nevertheless useful weapons in going into battle against it. In our part of the world, we have the ASEAN, which also provides a vehicle for regional cooperative efforts. Let us strengthen and make full use of these institutions and organizations. After all, it is merely stating a truism to say that the problems of an integrated global economy can be solved only within the framework of international cooperation.

STATEMENT BY THE GOVERNOR OF THE FUND FOR POLAND

Leszek Balcerowicz

Both my own country and the world economy have changed since I first spoke here at the outset of Poland's transformation in 1989. While I am proud to report to you that Poland remains firmly on the path of market-oriented reforms, macroeconomic stability, and sustainable growth, the recent developments in the world economy present a more complex picture. Economic turmoil often leads to intellectual confusion and false diagnoses, while demanding especially clear thinking.

Let me begin, therefore, with some clarifications. A lack of, or insufficient, controls on capital movements was not the primary reason for the present crisis in the affected countries. A simple comparison of these countries with those which have been resistant to the crisis reveals that the main reason for the differing performance is the quality of their macroeconomic, structural, and institutional frameworks for decision making. An appropriate response is therefore not increased controls, but rather improvement, of these frameworks through genuine reforms. Sudden outflows of short-term capital follow the periods of excessive inflows resulting from both imprudent lending and imprudent borrowing. The former points to the problems of decision making in large financial institutions; the latter reveals the deficiencies in countries' economic policymaking.

It would thus be totally wrong if the present crisis were to weaken the commitment to the basic virtues of openness, prudence, and arm's length relationships between politics and the financial and corporate sectors. These virtues have been vindicated by the recent developments. No effort should be spared to prevent the reversal of the generally beneficial trend toward open market economy and orderly liberalization of factor movements.

Globalization should not be the whipping boy in the debate about the current crisis. Globalization rewards those with responsible economic policies but carries risks for countries that avoid or delay reforms and disregard basic requirements of macroeconomic discipline.

After these diagnostic observations, let me move to the therapy. Two preliminary remarks are in order. First, one should distinguish between steps that are necessary to contain the present crisis, and measures aiming at prevention and containment of the future ones. These two sets of measures overlap to some extent but generally have very different time dimensions, with the former being obviously much more urgent. Also, while working on the containment of the present problems, one should not weaken and complicate the defenses against the future ones, for example, through unconditional bailouts of creditors or debtors. Second, factors that are given should be distinguished from those that can be treated as policy variables. The former include technological developments responsible for the speed of the short-term capital and the sheer size of these movements. There is no point in trying to control what is beyond anybody's control. In addition, these factors are not the primary reason for the present developments. It is not the mere speed and size of short-term capital but the policies of borrowers and lenders that are really relevant and should be changed, if necessary.

For the sake of brevity, let me focus on the issue of how to reduce the probability of future crises. The required strategy includes steps that are also necessary to deal with the present problems. I have here in mind, first of all, the economic policies of major industrial countries. Large countries have large responsibilities not only for themselves, but also for the world economy.

In thinking how to prevent the future financial crises I would mention two interacting mechanisms: first, better early warning systems that should be put at the disposal of governments, financial institutions, and the public at large; and second, measures to improve the quality of decisions made by the major players, that is, national governments, private financial institutions, and international financial organizations. The point here is how to ensure that sound policies are pursued and early warnings are not ignored.

Speaking about the first mechanism, I fully support efforts to enhance surveillance, increase transparency, improve data collection, elaborate and disseminate various standards, and make broader use of precautionary arrangements. I am glad to observe that basically all of this is already the work in progress in the IMF. While improving the early warning systems, we should know whether the present crisis in the affected countries resulted from the absence of early warnings or from early warnings that were sent but disregarded. It appears to me that the truth is closer to the second alternative. Whatever the exact response, the basic question for the future remains how to strengthen the foundations of policies that lead to sustained development and not to economic crises. It is basically a political question, as behind policies is politics, and financial crises have, in most cases, political roots. A major lesson from the present problems in the crisis-stricken countries is that intimate links between politics, financial institutions, and the corporate sector ultimately result in the mountains of bad debts and, as a result, in huge social costs. Also, one should think about constitutional arrangements that would limit fiscal deficits and the public debt. I am glad to inform you that such clauses already exist in the Polish Constitution, which was adopted last year. Finally, strong prudential regulations and strong supervision in the financial sector are of utmost importance. This is the main response to the complexity of modern financial markets.

I have focused so far on how to make the domestic policies more responsible and efficient. However, I also agree with those who see a potential problem in the behavior of private financial institutions on the lending side. Responsible decision making requires an adequate evaluation of potential risks, which, in turn, is inseparable from the penalties for the past mistakes.

Before concluding, I would like to make an official announcement that, I hope, should be well received by Mr. Camdessus. A week ago, on September 29, 1998, the Polish government adopted the resolution approving the proposed increase of Poland's quota in the IMF. This decision can be seen as a proof that my country is prepared to fully discharge its obligations resulting from the IMF membership and that we share the assessment that an early replenishment of the Fund's financial resources has become a matter of operational necessity. Pending any possible modifications of its future role and functions, the Fund cannot be left without resources allowing this institution to fulfill its current mandate and to provide assistance to countries in need. I call on all member countries to proceed swiftly with the agreed quota increase, and I urge the participating countries to speed up the adherence to the New Arrangements to Borrow. Poland is also ready to support the HIPC Initiative by depositing, on very beneficial terms, our share in the second Special Contingent Account (SCA-2) refund. We have already initiated the internal legal procedures leading to the approval of the proposed Fourth Amendment of IMF's Articles of Agreement, and I expect this process to be completed before year-end.

Statement by the Governor of the Bank for Portugal

Antonio de Sousa Franco

The world is facing an unexpected but decisive crossroad. The economic outlook has quickly deteriorated, and what began a year ago or so in East Asia as a regional crisis has spread to other parts of the globe and is threatening social and economic stability in many countries. Solidarity and equity, as well as freedom, suffer from that situation. Sound growth is more than always imperative, and we should keep on fighting for it with wise and successful policies.

As the Austrian President of the EU Council has said, developments in the EU have contributed toward international financial stability and sustainable noninflationary growth. The high degree of convergence among European economies and the effective beginning of the euro—a single European currency common to 11 countries—in less than three months have helped strongly to reduce market instability and to promote and preserve economic recovery. Today, in the world economy, the EU is a pillar of sustained economic growth and employment, reaping the rewards of stability and budgetary adjustment and contributing to long-term growth and employment. This concerted strategy is favorably influencing developments in the global economy but remains insufficient to eliminate the contagion effect. In a global world, crises tend to be global and demand global action.

An intense cooperative effort by all members of the world economy, both individually and at the regional and universal levels, is needed to find again the path to economic growth and employment. It should start with sound economic policies and strong structural reform programs, especially in crisis countries. Continued persistent implementation of reform programs should restore confidence, reverse the dramatic social and economic costs of the present situation, and lead to a resumption of resources to finance growth.

The international community is challenged to work hard toward reforming the global financial architecture with the aim of reducing the frequency and severity of financial instability and, whenever it occurs, dealing with it more effectively. The advent of the euro will be a major contribution by Europe to the smooth functioning of the international monetary system. The IMF should remain the centerpiece of the global financial system and should, in the short term, be provided with and create the accrued means to meet its responsibilities. However, although urgent and necessary, this is not enough from a long-term perspective. The global economy needs efficient and new global rules and institutions, and it is our duty to provide them.

We need a sound and transparent international financial system supported by better prudential supervision and efficiently regulated institutions, improved and expanded surveillance, and disclosure of transparent, accurate, and timely data. Attention has to be given to fostering an orderly and well-sequenced liberalization of capital movements. Sound financial sectors, strong supervision systems, and appropriate macroeconomic policies are preconditions for successful capital account liberalization. The IMF and the World Bank need to give these issues high priority, working more closely together and with others to assist members in managing more effectively the risks of global integration. However, the real social and economic costs of these crises have to go hand in hand, and the World Bank remains the key player in helping developing and emerging countries to reduce poverty and improve social welfare in a sustained manner.

Portugal supports the idea that—beyond immediate resources and programs—to deter fears and speculation, new times demand new horizons. A new Bretton Woods for the twenty-first century should be prepared, in order to generate new forms of political legitimacy, reinforce the governance of the IMF and the World Bank, restructure financial markets and institutions, and involve the states and the private sector in the resolution of the crisis and the full resumption of strong noninflationary growth. Many of us—all of us—agree with the principle, perhaps with the solution. Let us pass to action, immediately and strongly.

Finally, I would not like to end without a reference to the HIPC Initiative and to the needs of post-conflict countries. Portugal is glad to see that the initiative is well under way. I would urge members of the international community to ensure quickly the financing of the initiative. On the other hand, I would encourage eligible countries to pursue the adjustment programs to qualify for this assistance. Post-conflict countries face tremendous needs, and the international community has to be creative in responding to the challenge in a fairly shared and coordinated response.

Statement by the Governor of the Bank for the Russian Federation

Mikhail Mikhailovich Zadornov

When we met in Hong Kong a year ago, the first serious waves of the financial hurricane had already swept over East Asia. But I doubt that many of us foresaw the situation in which we would meet this time. Cautious optimism did not turn into reality—the crisis has deepened, striking more countries and destabilizing the financial and commodity markets to an even greater degree. The crisis has been transformed from local into global, and from financial into systemic.

As a result, the role of the Bretton Woods institutions becomes particularly important. They are expected to provide answers to a number of fundamental questions. They are expected to take decisive and broad actions designed to cope with the crisis.

Among the questions that face the international community and that directly concern the Fund and the Bank, the following especially stand out.

What Economic Policy Can Help Solve the Crisis While Meeting the Needs of Long-Term Development?

This question is a long way from being resolved. Most diverse solutions are being proposed—from currency board arrangements to suspending the current and even the capital account convertibility of national currencies. There is also a wide range of recommendations regarding fiscal policy. Countries affected by the crisis are advised, on the one hand, to drastically tighten their fiscal policy and thereby ease the pressure on the credit and currency markets, and on the other, to relax their fiscal policy just as drastically, so as to stimulate the economy and expand social welfare programs. Should we be tough and let the insolvent financial institutions go bankrupt in order to demonstrate impartiality or, conversely, should we support them, based on their systemic role in financial intermediation?

Without doubt, the ultimate responsibility for decisions on these and other issues lies with national governments. They make their choices based on local political realities and public preferences. Nevertheless, a clear and consistent position taken by the international financial institutions has an extraordinary, and often decisive, importance. Failure to formulate such a position, or inconsistency in carrying it out, could have a devastating effect on the reputation of these institutions. And this is true in the case of not only small and medium-size nations, but also the developed countries which play a leading role in the world economy.

What Are the Best Ways to Improve the Architecture of the International Financial System?

In our view, the best prospects for improvement lie in strengthening the national financial and banking systems, increasing their transparency, applying international standards, and upgrading the quality, timeliness, and availability of financial information. We agree with the main thrust of the international financial organizations' work in this area.

Unfortunately, the world community has done a poor job of learning lessons from the previous financial crises. As a result, the principal efforts now are focused, as in the past, on coping with the crises rather than on measures to prevent crisis-related problems. There remains a major unresolved question: what are countries to do if they have allowed short-term foreign capital into their markets without adequate preparation and without the appropriate conditions? Obviously, when there is a sudden and massive outflow of capital, these countries find themselves in a desperate situation and are often forced to take measures that meet with disapproval in the international community.

In other words, there is an urgent need to develop concrete and universally accepted mechanisms for dealing with such crisis situations. Specifically, we need internationally recognized procedures for considering issues of restructuring, defaults, and bankruptcies. In particular, in this context more headway could be made in solving the highly important problem of ensuring private sector participation in dealing with crises.

Are the Financial Capabilities of the International Institutions Adequate for the Demands of Combating a Large-Scale Crisis?

Unfortunately, the answer to this question is obvious. We face an immediate challenge—to ensure that the role and status of the international financial institutions are fully supported by the financial sources at their disposal.

We are alarmed by the fact that the Fund's liquidity has dropped to a critically low level. I believe it is essential, as quickly as possible, to complete the Eleventh General Quota Review, to approve the New Arrangements to Borrow, and to adopt the amendments to the Articles of Agreement on additional SDR allocation.

As for the Bank, we are concerned by the decline in its net income, caused both by an increased demand on its financial resources and by a diminishing profitability of its operations. On our part, we favor a carefully modulated approach to strengthening the Bank's financial stability. Such an approach should be based on the principle of fair burden sharing and should include both an increase in the cost of borrowing and restraint in the financing of new initiatives, strictest adherence to budgetary discipline, and greater utilization of earmarked funds. Unfortunately this approach has yet to find the support of the Bank's Executive Board.

The HIPC Initiative

The results that have been achieved up to this point confirm the viability of the initiative, and its effectiveness and considerable role in alleviating the hardships caused by the excessive burden of foreign debt. Since joining the Paris Club, the Russian Federation has taken part in measures implemented under the initiative to the greatest extent possible.

Nevertheless, we are troubled by the continuing rise in estimates of the costs associated with carrying out the initiative. The success of the initiative to a decisive degree hinges on its being fully backed by financial resources.

Cooperation Between the Bank and the Fund

In light of the latest crisis-related developments, cooperation must be strengthened between the World Bank and the IMF. In many areas, including the HIPC Initiative and reform of the public sector, both organizations have demonstrated the advantages of close coordination. Ultimately the Bank and the Fund have common strategic objectives. However, there is nothing surprising in the fact that, from time to time, we see an overlap of responsibilities, frictions, and even serious disagreements. We must not forget that there is a division of labor between the Bank and the Fund: while the Fund's efforts are aimed at maintaining macroeconomic stability and the efficient functioning of the international monetary and financial system, the Bank deals with specific projects, supports structural reforms, and places its emphasis on social issues and sustainable development. This division of labor seems fully justified.

In the Asian countries affected by the crisis, the Bank and the Fund failed to set up effective early coordination. At the same time, it is obvious that the nature of the crisis requires a qualitatively new level of cooperation between the Bank and the Fund. The proposal to establish a special Liaison Committee dealing with restructuring of the financial sector deserves particular support. This Committee should facilitate closer contacts between the Bank and the Fund. Moreover, it should be noted that a wider use of joint missions would not only help to optimize the utilization of both organizations' resources, but also promote a genuine culture of cooperation. The Managing Director of the IMF and the President of the World Bank were absolutely right when they pointed to the need for such a culture in their joint report.

What Has Happened in Russia?

Just a year ago, most observers shared the confidence of the Russian leadership that the most difficult period of economic reforms was over. We had managed to reduce inflation to a record low and to maintain a stable exchange rate for a long period of time. Signs of growth had appeared in the real sector of the economy.

The Asian crisis dealt a double blow to Russia. First, there was a drastic change in the overall attitude of investors toward developing and transition countries. Above all, this change affected short-term capital flows and led to extremely grave consequences for the stock markets and the government debt markets. Second, the sharp deterioration in Asia resulted in a steep decline of world prices for energy resources and raw materials. Revenues dropped not only for the Russian exporting industries, but for the budget as well. The current account turned negative for the first time since 1991.

The impact of these external factors sharply exacerbated domestic problems that had remained unresolved. The principal one among them is the extremely grave condition of the federal budget. An inefficient structure of budget obligations still persists in Russia, and the numerous attempts to reform this system have continually run into political difficulties. When production is declining and the tax system remains inefficient, the burden of traditional commitments becomes more and more onerous.

The global crisis has revealed the existing shortcomings of financing the deficit with short-term domestic debt. This debt was characterized by very short maturity and high real rates of interest. The relative accessibility of international short-term capital in 1996–97 led to a certain slowdown in public sector reforms.

The efforts to solve the accumulated structural problems have proceeded with great difficulty, above all in the area of government regulation of the financial and banking sectors, the energy sector, natural monopolies, and relations in the agrarian sector. The responsibility of economic agents in fulfilling their obligations, including those to the budget, has grown weaker as a result of inadequate efforts to apply legal means such as bankruptcy procedures.

We hoped—and I believe with good reason—that the restoration of economic growth would create more favorable conditions for solving all these and many other problems. Unfortunately, it turned out that Russia did not have sufficient immunity to global contagion. The macroeconomic stabilization that had been achieved was too fragile to withstand the shock of the crisis, and the domestic government debt market eventually collapsed, in spite of all the attempts by the government and the IMF to keep the situation under control.

As a result, we are now forced to struggle with the consequences of an unprecedented drop in the exchange rate of the ruble. We are making every effort to solve the domestic debt problem that erupted after August 17. At the very same time we must also act to restore the solvency of the banking system, normalize the national payments system, and revitalize tax revenues. It will hardly be news to anyone if I say that international assistance—above all from the Bretton Woods institutions—is absolutely essential for a successful resolution of these highly complex problems. We intend to maintain open and constructive relations with our partners, and we are counting on their understanding.

Statement by the Governor of the Bank for the Solomon Islands

Bartholomew Aba'au Ulufa'alu

I am pleased and honored to address the fifty-third Annual Meetings of the IMF and the World Bank Group on behalf of our Pacific constituency comprising the Marshall Islands, the Federated States of Micronesia, the Solomon Islands, Samoa, Vanuatu, and Palau, which is the latest member to join the Fund and the Bank.

The outlook for the world economy has deteriorated considerably over the past year, and as such it gives much cause for concern. Almost every country in the world has been affected—albeit to differing degrees. We in the small island economies have already felt the full weight of the Asian crisis. Many of us are concerned about reductions in tourist inflows, lower world commodity prices, and the decline in the volume of our exports. We have responded to the Asian crisis by strengthening our own macroeconomic management, and several of us have embarked on ambitious reform programs to improve the efficiency and effectiveness of government, strengthen government transparency, and facilitate private sector development.

We can learn from the mistakes of others and build stronger, more resilient economies. But given our limited resources, we also need financial assistance from bilateral and multilateral sources. And we need a more favorable international environment to get the desired response from such reforms. It is generally recognized that there is a deficiency in global demand, which needs to be revived. Otherwise, we will face the risk of a global recession. The issue of how to achieve an expansion in global demand is therefore very important.

While the industrial countries have the financial resources, we believe that the scope for pursuing expansionary fiscal and monetary policies in these countries is limited, because their economies are already operating at a high level of capacity utilization. Further injection of demand in these countries is therefore not likely to be very productive. On the other hand, there is a large deficiency in demand in the Asian economies, which are operating at low levels of capacity utilization. These countries need an urgent injection of demand supported by external funding to revive economic activity. How to achieve this is one of the biggest challenges facing the Bretton Woods institutions and the international community at this time.

Since many of the governments and business enterprises in the Asian region are highly indebted, their capacity to contribute to demand is very limited. It will, therefore, be important for multilateral institutions to assist the region in restructuring the debt so as to build some capacity for further expansion of credit in the short- to medium-term.

As small island nations, we appreciate and indeed support the principle of capital account liberalization. As a practical matter, however, we need a long transition period to achieve this. Our economies are very distinct from others. Our financial and other institutional structures are still underdeveloped and weak and our foreign exchange reserves are very low. Hence, we seek your understanding that capital controls may for some time remain an essential part of our economic management tool, at least in the current uncertain and volatile financial times.

We seek an early ratification of the Eleventh General Review of Quotas. We believe this will assist in improving the liquidity of the Fund, which in turn will benefit member countries in their endeavors to reform their economies. We also need to ratify the planned special allocation of SDRs to address the need to supplement international reserves, especially to avert the risks for a global recession.

It is a well-known fact that we are a community of countries that are geographically dispersed over a vast ocean with virtually no direct access to markets and with limited scope for economic diversification. As the recent Commonwealth Ministerial Mission to the international financial institutions emphasized, there is a need to promote understanding of the "small states paradigm" in the economic sphere. This is particularly relevant in the context of international trade. It is in this vein that the Bretton Woods institutions should give attention to the special attributes and constraints of smallness.

We support the efforts being pursued to improve Bank-Fund collaboration. However, this collaboration should aim to better serve members' development and balance of payments needs rather than be pursued for its own sake.

The current challenges facing our Pacific constituency members range from governance issues to tackling economic policy reform and meeting social welfare needs. We are determined not to be marginalized in the context of globalization. However, to achieve this, we need larger countries to also pursue their reforms aggressively. And we want a Fund and Bank that are sensitive and knowledgeable about our particular characteristics and forthcoming with technical and financial assistance when requested.

In concluding, I would like to thank the managements, the staff, and the Boards of both institutions for their constructive advice and assistance on behalf of my Pacific constituency.

Statement by the Governor of the Fund for Spain

Rodrigo De Rato Figaredo

The circumstances in which these Annual Meetings of the International Monetary Fund and the World Bank are being held are certainly very different from those that existed during our meetings last year in Hong Kong. In most countries at that time, growth rates were high and inflation was low, even though financial problems in Southeast Asia suggested that international economic trends might be viewed with a certain caution.

Such caution was justified; in fact, more countries are now affected by the upheavals in the international financial situation. The seriousness of events in the Russian Federation has increased the risks that this instability will impact other economies that—until very recently—were on the move and showed good prospects. The outlook for growth in the world economy has now diminished, even though the basic elements in many economies are in a better state than they have been for years.

Over the year, most of the more advanced economies have achieved satisfactory results; in particular, I wish to draw your attention to the economic recovery in the member countries of the European Union. This year, after successfully completing the convergence process required by the Treaty, 11 of the members embarked upon what is perhaps the most ambitious monetary project in the Union's recent history: adopting the euro as a single currency. Indeed, the international financial community is even now welcoming the new European currency as a decisive contribution to stability and growth in the world. At the same time, this monetary union entails assuming new responsibilities and participating more actively in the international arena.

Over the past few years, Europe has focused its efforts on achieving the necessary internal coordination for completing the project of establishing a single currency, but the international events now occurring require us to concentrate our attention on the process of international monetary cooperation. Europe, and the euro countries, must play an active part in defining the future international financial architecture.

Spain in particular is satisfied with the economic policies that have enabled it to become a full EMU member from the very outset. This has been achieved through large-scale fiscal consolidation measures that have imposed firm controls on public spending, especially as regards the structural component, reducing the government deficit from 7.3 percent of GDP in 1995 to 2.1 percent this year. Spanish society as a whole has joined in these efforts and supports Spain's role in the process of European integration. The credibility of this economic policy, the independence of the Bank of Spain, and a determined privatization policy have all helped control the inflation rate, which is currently about 2 percent.

In response to the new situation created by the single European currency, Spain has undertaken an extensive process of market deregulation and liberalization. Similarly, efforts have been made to promote investment in human capital, together with active employment policies. This series of economic policy measures, and the resulting confidence on the part of markets, has made it possible to substantially reduce interest rates, thus benefiting Spanish economic agents. As a consequence, growth is increasing, and employment is being created at a rate exceeding the European average. The good results achieved so far enable us to look forward with a reasonable amount of optimism. Nevertheless, developments in the international financial arena are making us prudent and moderate in our projections, and requiring us to speed up the process of stabilizing and liberalizing the Spanish economy.

Certainly, we can see some positive signs emerging in Thailand and Korea; however, instability in countries of the region may continue unless the Japanese economy begins to show signs of recovery. It is therefore the earnest wish of Spain, and of so many other countries, that the Asian nations should make progress along the path to economic recovery, and we are convinced that Japan must reform its financial system, increasing its transparency, and liberalize its markets, opening them up to competition. Japan is an essential element in the attempts to solve the international financial crisis.

The impact of the Asian crisis on world trade and commodity prices, together with the decline in confidence resulting from the Russian crisis, has damaged other emerging economies. In the case of Latin America, economic adjustment and political democratization have transformed economic life, setting the region on the path toward sustainable growth, without inflationary tendencies, and opening the way to the increased prosperity of its people. However, the contagion effect from the current financial crisis is reducing the availability of the financing necessary for the economies of Latin America. Spain believes that the international institutions must respond to this danger by providing the necessary liquidity for those countries that are implementing policies designed to achieve stability, economic liberalization, and financial transparency. The Latin American nations have made laudable efforts to modernize their economies. Those recurring episodes of hyperinflation, economic isolation, import substitution, excessive regulation, and inefficient monopolies have been left behind. Practically all the countries in the region have achieved a high degree of stability, openness, and competitiveness, and have implemented in-depth structural reforms, both in their financial systems and in their main productive sectors. It is essential for markets to appreciate the differences between these and other emerging countries. All of these efforts cannot—and must not—be swept away by the indiscriminate effects of the spreading international financial crisis. Spain regards coordinated joint support for the Latin American economies as a priority, and therefore the Spanish government presented to the recent meeting in Vienna of the Council of Economic and Finance Ministers of the European Union an initiative reasserting the need to strengthen coordination among the countries of the euro area so as to develop a joint response to the challenges presented by the international economy. The Spanish initiative also emphasizes our confidence in the economies of Latin America and their capacity to overcome market volatility. Spain supports the establishment of a new financial mechanism in the IMF that would provide additional support for these economies. We are making a firm political and financial commitment to this effort, and the government of Spain has already decided what our own contribution to it will be.

We are living in times of profound change. The existing architecture of the international monetary system was designed over 50 years ago, and must be overhauled and revitalized.

Spain believes that the International Monetary Fund and the World Bank must continue to be the main actors in the international monetary system. Both institutions—and particularly the IMF—need to be strengthened and provided with sufficient resources to enable them to carry out their functions in a globalized financial system. Moreover, we must ensure that participation in the governing bodies of these institutions is commensurate with the financial support provided by each member country. Yesterday, the Managing Director of the IMF proposed five principles for transforming the international financial system, and two amendments to the Fund's Articles of Agreement. Spain is ready to play an active part in these changes, which we must all cooperate in achieving.

We all agree on the urgent need to strengthen the banking systems in many countries, through the adoption of clear regulations and sound financial practices. We trust that the Fund, the Bank, and the other multilateral financial institutions will find ways to combine their efforts and coordinate their activities in order to address this most important issue.

In order to prevent future crises, it will be necessary to devise alarm signals for identifying risk factors, so that the necessary measures can be adopted in a timely manner. To this end, it will be necessary to further develop the specialized mechanisms that are already available to the Fund and the Bank, and those that have recently been established, such as the units for short-term surveillance and the monitoring of financial-sector operations. To resolve crises, joint action by both institutions is necessary, with the Fund focusing on macroeconomic equilibrium and the World Bank concentrating on the social impact of programs and on structural reforms—that of the financial sector being a priority. The Bank needs to design new products and to devise imaginative funding formulas in order to help countries carry out these reforms.

We hope that international capital movements will be liberalized in an orderly manner, and that the process will provide for at least elementary prudential standards. We are concerned to see that certain countries have unilaterally imposed restrictions on capital movements, and we trust that the Fund will soon be given effective jurisdiction to deal with this issue, so as to ensure that any interruption in the normal flow of financing will be the result of multilateral agreements that include clear provisions and precise schedules.

However, the implementation of economic programs also requires that countries continue to apply their policies for maintaining social cohesion and microeconomic modernization. Economic transformations are impossible without the support of men and women. This is why Spain supports the three-pillared approach presented by the President of the World Bank, Mr. Wolfensohn, for strengthening programs designed to maintain social cohesion and promote microeconomic activities in emerging economies. We must support the efforts of governments to make their economies more stable and open, but we must also ensure that schooling is provided for children, and that—in the emerging economies—small and medium-sized enterprises can expand.

We acknowledge the progress that has been achieved in disseminating economic data and increasing transparency in the activities of the Fund and the Bank. Nevertheless, we recognize that there is still much to be done, and we urge both institutions to redouble their efforts. In order for international financial markets to operate properly, they need a continuous flow of specific and relevant information.

It will certainly be necessary to make great efforts to establish a stable and transparent international monetary system. Whatever activities you undertake in order to achieve this objective, you can count on the support and encouragement of the Spanish government.

STATEMENT BY THE GOVERNOR OF THE FUND AND THE BANK FOR SRI LANKA

G.L. Peiris

It is my privilege and pleasure to address the fifty-third Joint Annual Meetings of the International Monetary Fund and the World Bank on behalf of the government of Sri Lanka, especially this year, as my country celebrates the Golden Jubilee of its independence. Mr. Chairman, let me join my fellow Governors in congratulating you on your assumption of chairmanship of the 1998 Annual Meetings.

World Economy

We meet at a time of considerable turmoil and uncertainty in the international financial markets, and the world economy is facing severe economic problems and challenges. International economic and financial conditions have deteriorated sharply, to a far greater extent than was projected at our last meeting. The period of recovery appears to be more protracted than anticipated. We are concerned that world economic growth, as well as the expansion in world trade, has slowed down sharply, and the short-term prospects are not encouraging. Recession has deepened in many Asian economies, resulting in heavy economic and social costs with spillover effects on other countries. The situation has been further aggravated by declining commodity prices, the Russian financial crisis, a sharp contraction of capital flows to low-income developing countries, as well as to emerging market economies. The capital market spreads have widened for all emerging markets and transition economies with no relationship to the countries' macroeconomic fundamentals.

Sri Lanka

Let me turn to my own country. Sri Lanka has managed to avoid the worst of the Asian crisis because many of the conditions that existed in the crisis-ridden countries did not prevail in my country. The policies in place and new policy responses helped mitigate, in substantial measure, the contagion effect. The domestic financial markets remained stable. The Sri Lankan economy grew by 6.4 percent in 1997, showing improved business confidence on account of significantly improved macroeconomic management. The unemployment rate continued to fall for the fifth consecutive year, and inflation declined sharply, reflecting the impact of our sustained efforts to improve price stability.

Even though some export products have been affected inevitably by the East Asian crisis, the provisional GDP estimate for the first half of 1998 indicated a 5.1 percent growth rate. Private investment is gradually improving, enhancing the growth potential of the economy.

Under difficult conditions, fiscal reforms are continuing. The overall fiscal deficit has been reduced consistently during the past three years by containing the growth of expenditures. The goods and services tax was introduced in 1998; as expected, tax compliance has improved, and the tax base has expanded. A large part of the privatization proceeds was used to retire public debt, with the beneficial consequence of reducing the government debt burden.

The balance of payments position improved, diminishing the current account deficit and augmenting the external assets position of the country. Our managed float exchange rate system and improved monetary management have helped maintain the domestic financial market in a relatively stable condition in a difficult external environment. In monetary management, we have increased our reliance on market-oriented monetary policy measures.

Despite challenging circumstances, substantial progress has been made in the implementation of structural reforms, because we strongly believe that they are of crucial importance in improving the country's economic performance and future prospects, and in strengthening the economy's resilience against external shocks. These reforms include several successful divestitures, further liberalization of foreign investment, continuing encouragement of private sector participation in infrastructure development activities, improvement in tax administration, tighter controls on government employment, and improvement of financial sector surveillance. The privatization program has been accelerated and extended into key areas such as plantations, telecommunications, and aviation.

In the political sphere, considerable progress has been made in the effort to reestablish normal life in the liberated areas in the north, the consolidation of the security situation, restoration of civil society in the north by the holding of elections and the revival of grassroots organizations, and the presentation to the parliament of a comprehensive constitutional reform package as a major step in the process of arriving at a political resolution of the ongoing conflict.

Bretton Woods Institutions

Turning to the Bretton Woods institutions, we understand the inclement environment within which these bodies have to operate today. We commend their efforts to help minimize the adverse effect of the recent crises. We believe that it is extremely important to have a more coordinated approach by international and regional financial institutions with private sector creditors to face the present challenges more effectively.

My country deeply appreciates the progress made with regard to the ESAF and HIPC Initiatives and the continuing assistance to post-conflict countries. We strongly support the continuation of these programs and encourage the Fund and the Bank to mobilize more substantial resources to fill the existing gap between financial requirements and available resources at present under the aegis of these programs. Country ownership as well as due recognition of country-specific situations are indispensable for ESAF programs to be more effective.

We commend the Fund for the steps taken to enhance its resource availability and its liquidity position through quota increases, SDR allocation, and augmenting of the new arrangements to borrow. I am acutely aware of the complex legislative initiatives required in member countries on these matters; I urge my colleagues here to complete these processes as rapidly as possible, as the Fund liquidity position has declined to an unprecedentedly low level, while the demand for Fund resources remains high. Quotas, which are at the heart of the operation of the Fund, should be increased as and when necessary to enable the Fund to play its role in the international economy. An early resumption of new SDR allocation, giving due consideration to the rising shares of developing countries in the world economy, is also essential in this regard.

We appreciate the initiatives taken by the Fund and the Bank to combat corruption and improve transparency and governance in all contexts, including their own activities. The preparation of a draft manual on fiscal transparency, publication of information on the Fund's liquidity position and activities, and encouragement of publishing more country-specific information are steps in the right direction. Similarly, we support Fund initiatives in respect of private sector involvement, especially with regard to forestalling and resolving financial crises, as burden sharing is improved. It is encouraging that the Fund is studying in detail the possible impact of introduction of the euro in January 1999 and related Fund operational issues, and closely working with the EMU to maximize benefits and minimize any potential risks.

We appreciate the Bank's financial assistance to crisis-ridden countries, notwithstanding its difficult financial situation. The crucial role of IDA in channeling assistance to low-income countries cannot be overemphasized in the context of continually declining ODA resources. We, therefore, urge the timely completion of the twelfth IDA replenishment process, which is now in its closing stages. We commend the expansion of IFC and MIGA activities, which are crucial to improving the private capital flows to developing countries, particularly in the present setting where private investors are showing greater inhibition. We strongly support improvement of closer Bank-Fund collaboration, as it enhances resource utilization efficiency and increases the effectiveness of programs. The importance of closer collaboration, given the increasing complexity of economic issues and increasing demand pressure on limited resources, should not be underestimated.

Strengthening the Architecture of the International Monetary System

Let me make a few concluding remarks on strengthening of the architecture of the international financial system. The process of globalization and recent financial crises in some parts of Asia, Russia, and previously in South America underscore the need to strengthen national and international financial systems. It is necessary to minimize the likelihood of crises in the future and to improve strategies and techniques for handling crises if they occur. A cooperative effort by all major players, that is, governments, the private sector, regional agencies, and international institutions, is necessary to address effectively such crises, as the impact may spill over from country to country and from market to market in a globalized economy, bringing about grave economic and social dislocation. Similarly, reforms should aim at achieving an appropriate balance between adjustment and financing and ensure that measures are in place to handle crises at their inception.

Statement by the Alternate Governor of the Fund for Switzerland

Kaspar Villiger

We all agree that the present situation of the financial markets gives rise to serious concern. Several countries have already suffered considerably under the current problems. We are here to discuss ways to resolve the crisis. I am afraid, however, that our deliberations have not contributed to calming the markets. In my view, many speakers tend to overdramatize the situation. About two-thirds of the world economy is in good health. In addition to that, the downward correction of the stock markets can be viewed as a normalization of exaggerations from the past. We must not create a depressed psychological climate that in turn could negatively affect the sound parts of the global economy. We need the growth of these economies to stabilize the current situation.

It is true that the present crisis has brought to light a number of structural problems in international financial markets. The problems have been identified. They now have to be addressed thoroughly and rapidly. However, there are no simple solutions and no quick fix. We will have to make strong efforts to solve the problems. I would like to propose a strategy comprising five elements:

- First, each country has to keep its own house in order and implement sound policies. Financial support should be given only to countries that in spite of sound policies have run into difficulties.
- Second, market participants must be in a position to assess the risk involved in their investments. Therefore, we need to enhance transparency.
- Third, it is imperative to involve private creditors in the solution of financial crises.
- Fourth, all this has to be achieved within the framework of the existing institutions. While these institutions must undoubtedly adapt to new challenges, they need to refocus their activities on their original mission.
- Fifth, before looking for new resources and facilities, the quota increase and the NAB have to be implemented.

Let me explain some of these elements in more detail.

Increasing Transparency

The ongoing efforts to increase transparency in all its dimensions must be stepped up. This is crucial to enhance the surveillance capability of the market. This in turn will help avoid abrupt changes in risk perceptions. Furthermore, transparency increases the accountability of the government and reduces the possibility for corruption. Through the development of appropriate codes and standards the IMF can play an important role in the promotion of policy and data transparency. At the same time, further steps should be taken to improve the transparency of the decision processes and policy recommendations of the IMF itself. The Bank can contribute to these efforts by increasing its focus on good governance and corruption in its country strategies and through appropriate project design.

Strengthening the Financial System

The IMF and the World Bank need to continue to give this issue high priority. The task is too complex to be mastered by one institution. Therefore, the Fund and the Bank have to cooperate closely. I welcome the efforts and specific proposals that have been made to enhance this cooperation.

Involving the Private Sector

We must work hard to find solutions to involve the private sector in resolving financial crises. In searching for a solution, we should try to include all actors, including the private sector. This is necessary not only for equity reasons or on grounds of the social and political acceptability of the actions of the Bretton Woods institutions. It is also important because of the lack of public resources to deal with liquidity crises in globalized financial markets. However, the scope for a voluntary involvement of the private sector is limited. Unilateral debt moratoriums may therefore be unavoidable. A backing by the Fund could help to minimize the damage of such measures and ensure that the debt-restructuring process be as orderly as possible.

Refocusing on the Original Mission

The recent crises have required massive liquidity support from the IMF, the World Bank, and member countries. Even for the IMF such use of resources is difficult to reconcile with its mission. It should exercise primarily a catalytic role. Emergency liquidity support is even more difficult to justify in the case of the World Bank. Clearly, this is not the primary responsibility of the World Bank. Its main focus in crisis management should be on measures to address the social consequences of the crisis on the poorest and on the subsequent more far-reaching structural reforms.

Securing Financial Resources

The IMF and the World Bank can take a lead in the prevention and resolution of crisis situations only if they have sufficient resources. The lending in the past year has led to a serious deterioration of the resource bases of the IMF and the IBRD. The IMF quota increase must become effective as soon as possible. The current global situation also makes an enhancement of the IMF's financial safety net essential. Therefore, the New Arrangements to Borrow should rapidly become operational. Furthermore, if emergency financing of the World Bank is to continue, measures must be found to ensure its capacity to contribute. Otherwise, these lending operations could limit available capital for lending to developing and transition countries and increase lending costs. Furthermore, the World Bank's capacity to contribute to IDA and the HIPC Initiative could be reduced.

To conclude, I want to underscore the fact that the particular attention emerging market economies have received over the past year should not lead us to neglect the other members of our institutions. Smaller transition countries continue to require the support of the IMF and the World Bank in order to ensure that the initial reform progress maintains its momentum. The same is true for lowest-income countries. Securing the financing of the continuation of the Enhanced Structural Adjustment Facility, IDA lending, and the joint HIPC Initiative must remain at the top of our agenda.

Finally, the Fund and the Bank should be commended for their good work and in particular the prompt response, the negotiation of programs in record times, and for mobilizing the necessary financial resources. The crisis is putting a considerable strain on the staffs of both institutions, and their efforts and achievements must be acknowledged.

Statement by the Governor of the Bank for Thailand

Tarrin Nimmanahaeminda

It is a great pleasure and privilege for me to address the Annual Meetings of the Boards of Governors of the Fund and Bank in Washington, D.C. this year. Since the last Meetings in Hong Kong, the world economy has deteriorated significantly. The effects of the currency and financial crisis in East Asia have spread not only within the region, but also to markets as distant as Russia and Latin America. Continuing turmoil in international financial markets raises the specter of a meltdown at the global scale. It is time for decisive international policy coordination among both developing and developed countries, as well as by the multilateral financial institutions. Previous speakers have already pointed out the precarious world condition, and I will limit my presentation to a few issues involving my country.

Being the first to slip into crisis, Thailand is destined to be one of the first to get out. We realized fully well that this will only be possible through a comprehensive reform program supported by the international community. I will briefly review the progress we have made. I will discuss the causes, the responses, the immediate problems, and the risks. I will finish with a few observations about the Fund and the Bank.

The Causes

I consider three factors to be the causes of the crisis that erupted in Thailand last year. First, on the fundamental, the current account has been in a large deficit for a number of years. This has been fueled by huge capital inflows as local corporates made use of foreign resources without adequately taking into account exchange and market risks. At the same time, the banking system has not been prudent in assessing credit risks. When exports did not perform as expected in 1996, the stock market reacted negatively, thus causing double runs in the currency market and the financial institutions. Second, in response to the runs, the authorities did not pursue appropriate policies in coping with the speculation on the currency and the liquidity problem of the financial institutions. They defended the baht up to the point of depleting the reserves and aggressively made use of public funds to support the insolvent financial institutions. Third, when the actual magnitude of the net official reserves was disclosed for the first time in August 1997, the market panicked. Even though the government came up with a strong stabilization program supported by the IMF, it did not regain confidence, particularly as the credibility of the policymakers was in question. This probably sent the strongest shock wave on transparency and accountability problems and thus became a contagion effect.

The Response

With the new government installed in mid-November last year, Thailand has responded to the crisis by strictly adhering to the comprehensive reform program. Apart from aiming at stabilizing the macroeconomic setting, it includes restructuring of the financial system with strengthened supervision, corporate debt restructuring, amendment of the legal framework, promotion of good corporate governance, privatizing of state enterprises, and the further opening of the economy. Moreover, social programs to address the plight of the underprivileged have been initiated and put in place. To regain confidence and reverse the steady downward trends of both the stock market index and the currency value, the government has undertaken policies based on the following principles: stabilization, transparency, the private sector's own initiative in external debt management, and maintenance of an open economy policy.

First on stabilization, we placed a high priority on stabilizing the economy by pursuing cautious monetary and fiscal policies, including inducing short-term interest rates at levels consistent with exchange rate stability; sourcing foreign funds from multilateral and bilateral agencies; restructuring the financial sector to reestablish depositor confidence, and arranging dedicated lines of credits for exports and other key sectors.

Second, we attach great importance to transparency as a critical means to shore up market confidence and impose policy discipline on the officials, in particular, the dissemination of information, such as the letter of intent and statistics in line with the IMF's Special Data Dissemination Standard. For example, net official reserves is announced on a weekly basis.

Third, on private initiative, it is important to note that in managing the external payment accounts during the crisis period in the past 15 months, the private sector itself has been the prime player both in mobilizing or allocating investment and in arranging the settlement or rollover of their obligations. The government has resisted a call for interfering either directly or indirectly, and is thus preserving the voluntary nature of external debt settlements among the private sector. This is thus consistent with the market-oriented character of private financial activity in Thailand.

Fourth, in working out the crisis and laying the basis for reform, Thailand has strictly adhered to the principle of openness and rejected any pressure for protectionism. We have not resorted to administrative means to replace the market mechanism. In contrast, opening market policy constitutes a prominent part of our latest reform program.

Despite a difficult external environment, these measures have successfully restored stability. The current account is no longer in deficit. It has reversed from a deficit of about \$1.2 billion per month to a surplus of about \$1 billion per month in 1998. Net international reserves position increased to \$15 billion in September 1998. Nearly all the external swap obligations with foreign banks abroad have been unwound, with only a few hundred million U.S. dollars left. Gross reserves now account for 7.2 months of imports and are able to cover the total short-term external debt. The currency that has depreciated throughout 1997 had appreciated from over 55 baht/\$1 in January 1998 to about 40 baht/\$1 in the first quarter of 1998 and has been stabilized ever since. We have also been successful at restraining inflation which, having already peaked in June, is estimated at about 9 percent for this year. Consequently, short-term interest rates declined markedly from over 20 percent in January to less than 7 percent in September.

The Immediate Problems

Despite the stability in the macroeconomy, the internal working of the real and financial sectors has become a major problem. The real sector is starved with credits as the banking sector becomes excessively risk averse while nonperforming loans expand rapidly. This in turn induces private borrowers to refrain from honoring their obligations and exacerbating the nonperforming loan problems. We have to break this vicious circle.

We are addressing the nonperforming loan problem in several ways. The central point is private debt restructuring. We have introduced new rules governing nonperforming loan exit procedure based on international standards. We provided tax incentives for debt restructuring. Our recently announced capital support facility also provides direct incentives for debt restructuring. We set up a high-level committee to facilitate the debt restructuring process using a market-based approach. We are fully cognizant that the debt restructuring process needs to be complemented by effective supporting legislation. For this reason, we are in the process of amending key foreclosure and bankruptcy legislation, which we expect will be enacted this year.

To strengthen the financial sector, first, we have required all financial institutions to submit a plan for their capital increases under memoranda of understanding with the Bank of Thailand. Second, we have gradually tightened loan classification and provisioning standards in line with international practice. Third, we liberalized the limit on foreign equity in financial institutions. Furthermore, as part of our process to improve the operations of the Bank of Thailand, we have brought in experts from central banks of industrialized countries to support a high-level commission in developing recommendations for strengthening central banking and bank supervision in Thailand.

Higher provisioning requirements due to tighter standards and declining asset quality, however, have caused financial institutions to become increasingly capital constrained and restricted their ability to lend. At the same time, the deteriorating economic environment has made it very difficult for financial institutions to raise private capital on their own from both domestic and foreign sources. For this reason, the government announced a financial sector restructuring plan on August 14 that included two capital support facilities totaling 300 billion baht. In partnership with private investors, we will recapitalize financial institutions by exchanging government bonds for preferred shares and subordinated debt. These facilities are structured to catalyze the entry of private capital as well as to facilitate new lending and corporate debt restructuring. Both facilities build in appropriate safeguards for the use of public funds. The new capital injection will be on a preferred basis, and the government or new investor will have the right to replace management. The burden on public finances will be minimized by requiring the preferred shares and subordinated debt to yield a return higher than the interest payments on the government bonds.

Policy Shift

With the achievements in stabilization, a more solid basis for the resumption of economic activity is now established. We have phased in measures to stimulate aggregate demand to contend with the sharper than anticipated economic contraction. The depressed state of Asian economies, coupled with widespread currency devaluation among our competitors, suggests that a large increase in export demand is not likely in the near future.

As a consequent of the financial crisis, domestic private demand for consumption and investment has dropped substantially. The burden of raising aggregate demand therefore falls heavily on the budget. Concurrently, we are creating training and employment programs to mitigate the labor problems. Government spending is the most direct means to strengthen the social safety net and mitigate the impact of the crisis upon the poor. We have obtained support from development agencies to provide both financial and technical supports to take care of the social dimension of the crisis. Consequently, Thailand gradually relaxed its fiscal stance for fiscal year 1998 from a public sector surplus of 1 percent of GDP at the outset of the program in August 1997 to a deficit—excluding the cost of financial sector restructuring—of 2 percent and 3 percent in February and May of this year, respectively. To stimulate further the economy, the government will continue to maintain an overall public sector deficit of about 3 percent for fiscal year 1999. Nevertheless, this will be self-correcting as the economy rebounds and should not create a structural deficit.

To stimulate private demand, we have also gradually lowered interest rates in a manner consistent with maintaining exchange rate stability. However, the critical factor to restore the health of the real sector is to induce the banking system to resume its intermediary role with the measures I have outlined above. We have also tried to ensure that critical sectors such as exports, housing, agriculture, and small-scale industries receive adequate credits through state-owned specialized financial institutions. We have mobilized funding particularly from both the official and private organizations abroad for this purpose.

The Risks

Thailand has done its best to establish a solid foundation for a rapid and sustained economic recovery. Our comprehensive reform measures should allow the economy to return to positive growth in the coming months. We are endeavoring to implement the measures within the time frame stipulated in the program. However, in the current global environment, there is little doubt that external conditions will continue to be critical for the recovery of Thailand and other countries in crisis. In this context, I would like to invite all the stronger economies to undertake a global solution in supporting the world economy in at least four ways.

First, the demand management policies of the major countries should be well orchestrated to avert a world recession. More important, maintaining an open market for trade is fundamental to assist the debt-trapped emerging countries.

Second, it is now extremely difficult for emerging economies to source funds from private international capital markets. The G-7 governments should therefore consider extending assistance to induce capital flows to those countries in crisis. I would like to praise Japan for the Miyasawa scheme in providing bilateral support to Asian countries for promoting reform and facilitating recovery.

Third, a system needs to be put in place for monitoring, if not regulating, cross-border short-term capital flows, which should help us understand their scope. This could enable us to mitigate the adverse effects from volatile capital movements. Recent events have highlighted not only the excessive leverage and exposure of highly speculative hedge funds and their threat to disrupt markets, but also the lack of adequate disclosure and regulatory standards.

Fourth, G-7 countries should support the People's Republic of China in its role as an anchor of economic stability for Asia. The stability of the Chinese currency is a necessary condition for the stable economic environment in the region.

Let me now turn to the important role of the multilateral financial institutions at this difficult juncture. I have participated in the G-22 working groups, and I would like the Bretton Woods organizations to consider carefully the recommendations made by the three working groups in shaping a new architecture for the world economy. Now let me turn to the immediate matters regarding the roles of the World Bank and the Fund.

IBRD Matters

On Bank matters, the crisis has underscored the extreme volatility of private capital flows and the importance of official resource transfers. Supplementing resources to strengthen the World Bank is crucial. I urge the donor community to do their utmost in replenishing the IDA. This is vital to ensure that the poorest nations would have sufficient resources available to cope with the upcoming difficulty. While pursuing this difficult task, the World Bank must maintain its triple-A status in the capital market.

IMF Matters

Turning now to Fund matters, I welcome the establishment of the Supplemental Reserve Facility to address large short-term financing needs. In addition, in view of the low liquidity levels, I urge all members to consent quickly to the Eleventh General Review of Quotas. We should also quickly accept the Fourth Amendment on the special one-time allocation of SDRs. These all should help enhance the effectiveness of the Fund to cope with the new challenge ahead.

Final Remarks

I would like to conclude by commending the two Bretton Woods institutions for their speedy, flexible, and decisive responses to the crisis. I wish to thank them for their roles in working with us in Thailand throughout the crisis in the past year. Their ability to marshal international support, including their policy advice and financial resources, has been extremely useful in helping us to cope with the crisis. It also underlined the continuing importance and relevance of these institutions. They have fulfilled, and possibly exceeded, the role that was envisaged for them by their founders some 50 years ago. The current crisis provides them with an important opportunity to define further their role in the global arena. With decisive action on the part of the multilateral financial institutions, G-7, and the countries in crisis, I am confident that we can jointly overcome the difficult challenges facing us today.

STATEMENT BY THE GOVERNOR OF THE BANK FOR TONGA

Kinikinilau Tutoatasi Fakafanua

It is an honor for me to represent the government of the Kingdom of Tonga at the 1998 Annual Meetings of the Boards of Governors of the World Bank and International Monetary Fund.

The year 1997/98 has been a very challenging year for most member countries. The financial turmoil in Asia that erupted in mid-1997 has left many Asian economies with currencies and asset values far below precrisis levels. Moreover, the crisis has resulted in a slowdown in global economic growth during the year. Among the advanced economies, the outturn for Japan has deteriorated further. Fortunately, economic growth in North America and Western Europe has been sustained and appears likely to remain so in the period ahead. The robust domestic conditions in these economies should facilitate the adjustment of current accounts in those emerging Asian markets affected by the sharp declines in capital flows.

Turning to the Pacific region and, in particular, the Kingdom of Tonga, growth performance over the past decade has been mixed. Tonga experienced average GDP growth in excess of 4 percent during the early 1990s, but this has not been sustained since 1995/96. A combination of factors, such as the slump on commodity prices of exports like vanilla and adverse weather conditions affecting other exportable agricultural production, have been the main causes. As a consequence, we are now faced with a substantial trade deficit. The expansion of the banking system has brought about a surge in domestic credit that is now approaching unsustainable levels, spiraling an acceleration in import demand, and causing the gross official foreign reserves to deteriorate below acceptable levels. The overall level of inflation, however, continues to be about 3 percent.

Notwithstanding the above constraints, however, we are committed to our objective of stabilizing and restoring growth to our economy. On the fiscal front, we place priority on improving the overall incentive structure for exports, and hence the balance of payments. We are also pursuing a balanced (recurrent) budget by adopting a central strategy aimed at rationalizing expenditures, while at the same time expanding the revenue base. Progress on the public sector review program has now been made, and greater emphasis is being placed on establishing tax and tariff structures that are less distortionary and at the same time conducive to productive activity. In particular, we are pursuing a more broad-based tax structure as the main source of revenue.

The rapid erosion of international reserves warrants further monetary tightening, and our monetary authorities have taken measures to improve the supervision of the banking system to ensure its long-term viability and stability. We acknowledge the continued efforts by the Bank and the Fund in providing appropriate policy advice, and we consider the annual Article IV consultations to be essential and important in supporting our efforts at economic stabilization.

Turning now to Bank and Fund matters—capital flows to our region, in terms of aid and concessional loan resources, should not be affected by the financial crisis in Asia and the recent turmoil in Russia. We note that total flows of ODA to developing countries have continued to decline. In 1997 ODA flows averaged 0.22 percent of GNP for the countries of the OECD as a group, reflecting a long-term decline from 0.33 percent in 1992. The Bank and the Fund are therefore urged to ensure that the level of aid assistance to small member countries is maintained in real terms. The Bank's agreement to collaborate with the Commonwealth Expert Group in the development of an acceptable vulnerability index for use when considering the graduation of member countries from concessional sources of financing is commended.

We support the call by the Fund and the Bank for concerted efforts to respond to member countries in crisis. The effects of the Asian crisis, the recent turmoil in Russia, and their spillover to other markets have imposed substantial costs on individual countries and on the world economy as a whole. This underscores the need to address policy weaknesses at the national level at an early stage and the importance and urgency of the Fund's work on the proposed revised international architecture. We acknowledge that progress has been made on several fronts, including substantial financial assistance to underpin stabilization measures and programs of structural reform and technical assistance in key sectors. In this regard, we welcome the move to strengthen the Fund's surveillance activities. We would also like to endorse the call for involving the private sector in resolving and forestalling crises and welcome the initiative of the Bank to provide financial assistance to address the global problem of the millennium bug.

On the ESAF and the HIPC Initiative, it is important that we continue to respond to the needs of our poorest members who are adversely affected by the downturn in global economic conditions. On the IMF quota increase, we endorse the need to increase the Fund's resources in order to cope with the difficult tasks ahead.

In conclusion, I believe that the lessons learned from the recent events and the policy responses currently established will ensure a successful transition to the new millennium. I call on both the Bank and the Fund to accelerate efforts to restore global economic stability and growth and to ensure that all member countries are accorded appropriate assistance during times of increased uncertainty. Finally, I wish to thank the Managing Director of the Fund and the President of the Bank and their staffs for their tireless efforts during the past year and to reaffirm our continued support during this difficult time.

Statement by the Governor of the Fund for Turkey

Gunes Taner

As the Managing Director of the Fund observed in a recent speech to the European-American Council in New York, we are now in the midst of an era of globalization. The economies of the world are rapidly being integrated in unprecedented ways. Financial turbulence has prompted the creation of a forum for discussing common regional issues and exploring remedial policy actions that can lead toward a new international monetary system.

We view the present Annual Meetings as an especially timely gathering from the standpoint of the worldwide financial crisis now going on. As we all know, the contagion effects of the Asian crisis have been severe for both individual regions and the world as a whole. The latest developments in the Russian Federation show that not only the Asian countries, but countries elsewhere, are exposed to the consequences of this crisis. All nations are put on notice that contagion effects may test their fundamental economic health and their vulnerability to market volatility. This is a time of serious challenges to the sustainability of world growth and countries' structural adjustment efforts.

The world growth projections of early August have again been revised downwards. Most of this slowing results from renewed instability in Asia's financial markets, renewed financial turmoil in the Russian Federation, and their contagion effects on other countries. Some market observers are already evoking the grim specter of a worldwide recession. It is evident that in today's integrated economic and financial world, the domestic policy weaknesses of one country can threaten the stability of all.

Now, the contraction of market financing is beginning to penalize emerging market countries in particular; the shortage of financial flows to these countries is their major challenge. Their balance of payments will come under pressure, and their growth will inevitably slow in the absence of effective and concerted countermeasures.

The right signals must be sent to the international capital markets, who must stand firm in the face of the present turbulence. Otherwise the outlook for world growth and prosperity will be gloomy and progress toward an open world trading system with free capital markets will be stalled.

It is especially important, given countries' increased openness to international capital movements, to restore the stability of international financial and exchange markets. This is one of the main issues to be addressed at these 1998 Annual Meetings. The Asian and Russian crises have directed much attention to fixed exchange rate arrangements and capital account convertibility, issues which are also important to Turkey. Although a pegged exchange rate is useful as a nominal anchor when bringing down high inflation—as Turkey's experience shows—a more flexible policy is preferable for open economies once they have been stabilized and growth has resumed.

The trend toward openness and liberalized capital movements has been good for the world economy. Once a country decides to liberalize, the temptation to reimpose restrictions that may backfire in the longer run should be resisted. Stop-and-go liberalization is to be avoided by taking care to carry out the liberalization process at the right pace and in the proper sequence, and to reinforce it with a further strengthening of the macroeconomic policy framework. Premature liberalization can require a very costly reversal of the process.

We see a significant role for the IMF and World Bank in assisting countries to liberalize capital movements and believe that the future well-being of global financial markets could be enhanced by an international commitment to promote orderly capital account liberalization in the long term.

We also favor amending the Articles of Agreement to permit a special one-time allocation of SDRs. This long overdue agreement will double the present amount of SDRs and equalize the SDR-to-quota ratio of all members.

Ever since the Mexico crisis, the Fund has been scrutinizing the adequacy of its surveillance, and has taken steps and launched initiatives to strengthen data quality and dissemination, providing a more solid basis for decision making and increasing its transparency and accountability.

Changing circumstances now call for the IMF's role to be strengthened and redefined. Effective surveillance over financial sector issues will be helpful. The Bretton Woods institutions should make stronger efforts than ever before to mobilize available resources in order to prevent present conditions from permanently destabilizing world markets.

I also wish to commend the IMF and the World Bank for their cooperative efforts to launch the initiative for reducing the debt of the heavily indebted poor countries. The main challenge now will be for the eligible countries to implement their programs and for financial institutions, public and private, to mobilize financial support.

It is important to provide the IMF with adequate resources to fund future drawings of member countries as the volume and scope of private capital movements increase.

Let me take this opportunity to say a few words about the Turkish economy. During this time of turmoil in Asia and Russia, Turkey is addressing all the key issues requiring priority attention under its staff-monitored program (SMP) with the Fund. We are strictly implementing the SMP to ensure that all targets and benchmarks will be met.

Turkey has made important progress with privatization in 1998. This is the first year, since privatization began over a decade ago, that Turkey has managed to complete about $2 billion.

This year's fiscal revenues are expected to exceed 20 percent of GDP. In the structural area, Parliament has approved a tax reform package that will broaden the tax base, close loopholes, reduce collection lags, and lower taxation rates.

We believe that Turkey has responded appropriately to the turmoil in emerging markets and tensions in its own domestic debt market by substantially tightening its fiscal stance, which in fact has led to a larger than expected increase in the primary surplus. Fiscal tightening at the first shock was the single most important reason for Turkey's so far successful resistance to the present turbulence.

The government intends to follow the economic program closely and keep its pledge to meet all targets under the SMP. Continued efforts against inflation will also strengthen the economy against external shocks. Turkey's geographic location will give it a special importance in an era when energy resources will assume a decisive role in determining world prosperity.

Statement by the Governor of the Fund for Turkmenistan

Yolly A. Gurbanmuradov

Delegates to this Annual Meeting have made many proposals to improve the operation of the international monetary system. Understandably, many of these proposals are directed to improving the future operation of the system. However, in this short intervention, Turkmenistan wishes to emphasize that there is an urgent need to deal with the emerging contagion problems of the present crisis, particularly in Commonwealth of Independent States countries, before moving on to deal with desirable future changes to the system.

The Turkmenistan authorities' particular concern relates to the nonpayment of intergovernment arrears within the CIS countries. As at the end of 1997, Turkmenistan was owed $1.3 billion by other CIS countries, mainly in respect of nonpayments for past gas shipments. Over recent years, Turkmenistan, with Fund encouragement, has agreed to reschedule payments of overdue amounts to facilitate orderly adjustment by our debtor countries such as Georgia and Ukraine. This rescheduling was made in good faith and at a considerable cost to Turkmenistan. However, with its own exports now under pressure from both falling commodity prices and political and other difficulties in transporting gas to traditional markets, Turkmenistan now finds itself in a very difficult external situation.

We are now no longer in a position, therefore, to provide what amounts to "forced" balance of payments, support to our neighboring countries, the more particularly so as our past actions of support have been badly abused by some of our debtors who now choose to spuriously dispute their debt obligations in the hope of delaying or avoiding repayment obligations.

Recently, we have seen the situation worsen considerably with debtors, such as for example Georgia, defaulting on agreed principal repayments despite the presence of a Fund program which should have required the countries concerned to meet debt obligations. In short, Turkmenistan is facing a clear case of financial contagion arising out of the failure of Fund programs to restore financial viability to our major trading partners within the CIS region. While the Fund has sought to assist in resolving these problems by requesting the countries concerned to reschedule debt, it nevertheless approved a further extension of Georgia's ESAF loan agreement this year without requiring a resolution of its unpaid debt obligations to Turkmenistan. We fear that similar situations could arise with our other debtors, notably Ukraine, which now face severe strains as a result of the Russian crisis.

In our view, these unsatisfactory payment procedures require immediate attention in any discussions of reform of the international monetary system. Just as it has sought to assist the orderly rescheduling of debt for western bankers involved in lending to Asian countries, so the Fund must require debtor countries within the CIS region to sit down with their creditors, such as Turkmenistan, and agree on firm repayment schedules. It should be a condition of these discussions that failure to adhere to such payments should incur sanctions in the form of program suspension or some similarly severe punishment, such as penalty interest charges on Fund loans. If the Fund feels it necessary to overrule such sanctions, compensatory financing should be paid to the creditor country involved from the Fund's own resources.

It should also be recognized that these agreed repayments should receive priority over other debt payments, such as servicing of commercial loans from overseas banks. We have seen evidence that many of these commercial loans were based on speculative transactions rather than genuine trade or development financing. Moreover, we are most concerned that the cross-default clauses often embodied in these loans add enormously to the financing of any rescheduling of debt (as for example has occurred in the case of Ukraine). The funds recouped by the insertion of such clauses by legally advantaged western bankers are then denied legitimate trade financiers, such as Turkmenistan. It would be most unfair to see relatively poor countries disadvantaged in this debt resolution at the expense of legally advantaged speculators.

Without such measures, we fear that there will be a collapse of the payments system within the CIS region and the problems seen in one country of the region will quickly spread to others, leading the whole region to become immersed in economic crisis. Turkmenistan appeals to other delegates present at these meetings to give urgent attention to these crucial payments system issues in their discussions of desirable reform of the international system.

Statement by the Governor of the Bank for Ukraine

Valeriy Pavlovych Pustovoitenko

The delegation of Ukraine to the Annual Meetings welcomes the business-like character of the discussion on the ways to prevent the financial crisis in emerging markets from evolving into a world economic crisis. Yet the crisis became virtually overwhelming for emerging market economies, and no one can state with certainty how long it will last. In these conditions the government of Ukraine believes that the only possible way out is by accelerating structural reforms, adjusting our budget expenditures to the possible noninflationary sources of funding, and continuous work with private creditors whose contribution we appreciate; we are grateful as well for their understanding of our short-term liquidity problems. We are confident that the low—compared with the export and GDP—level of accumulated debt and the reforms that we implement will increase our creditworthiness and financial capacity. We are grateful for the timely support from the international financial organizations and appreciate the timeliness and effectiveness of their financial and technical assistance.

According to our estimates, the orderly implementation of the recently approved IMF Extended Arrangement and the project portfolio prepared together with the World Bank will reduce the negative impact of the regional crisis on the economy of Ukraine and speed up the market transformation process. Ukraine, together with the IMF and the World Bank, has found a way to overcome temporary difficulties. At the same time, a coordinated action plan in case of a crisis spillover remains essential for all the economies in transition. We would like to propose speeding up the preparation of standards for the international community's schemes for private sector involvement in crisis prevention and resolution, in the context of a well-considered capital account liberalization on a nondiscriminatory basis. It is our belief that it would be impossible to design a new architecture for all constituents without the most active involvement of the World Bank and the IMF, organizations with an almost universal membership. This architecture will prevent financial destabilization from spreading from one country to another because of a lack of confidence by separate groups of investors not taking the macroeconomic situation in these countries into account. Only the IMF and the World Bank, and not any other entity, are capable of designing a new architecture for the world monetary system. As one of the largest recipients of the World Bank and IMF technical assistance, Ukraine believes that the opinion of resource recipients should be given consideration while discussing any plans of reforming those institutions.

We believe that economic growth, recent statistical signs of which can be observed in Ukraine, can be explained by the fact that parts of the shadow economy are coming into the official sector. This was stimulated by the deregulation measures drafted jointly with the World Bank and IMF and by actions to enhance openness and transparency and improve the quality of the overall system of governance. In this context we actively support every initiative to enhance transparency and openness of information in the budget area as well as in the financial sector.

The year we left behind was a year of big challenges for the international organizations as well. It is worth mentioning that we in Ukraine carefully followed the ways in which these institutions confronted some of the most significant challenges in their history. We were impressed by the words of President Wolfensohn on the first page of the Annual Report of the World Bank: “For all of us at the World Bank Group, the crisis has highlighted the fact that financial and social policy must go hand in hand.”

Speaking of our collaborative programs, they were highlighted by this very kind of unity. Together with the World Bank staff, we concentrated our attention on the key directions of the structural reforms: development of enterprises, agriculture, the energy sector, and the financial sector, and addressing ecological problems. Despite the somewhat uneven pace of our program with the Bank, we can state with confidence that we achieved great progress in understanding the goals and tasks that we are facing, and in implementing the mechanisms that are necessary to achieve them.

We cannot but be alarmed by the problem of the lack of funds in the international financial organizations, and by the income dynamics of the World Bank, in particular. During the past year the Bank successfully proved its usefulness to all of its shareholders, borrowers and nonborrowers alike. Yet, today we observe that all attempts to improve the present financial position of the Bank come as a burden on the shoulders of the IBRD borrowers only. In this respect we encourage all the members of the World Bank Group to look for a comprehensive solution to the income problems, including the possibility of a general capital increase. We also hope for the expedient adoption of the current quota increase of the Fund. The sooner we accomplish it, the sooner we will be able to come back to the appropriate financial standing of the institutions.

We are glad to observe the signs of the qualitative expanding of the International Finance Corporation activities. We believe that in Ukraine this institution will find more areas to apply its financial instruments and experience in employing the contemporary methods of private sector management. It is hard to overstate the role that the IFC can potentially play in catalyzing foreign direct investment and accelerating the development of the private sector in Ukraine and other countries.

We would also like to commend the efforts of the Economic Development Institute, the Joint Vienna Institute, and the IMF Institute, which are well known in our country. The initiative for economic education and training of officials launched by these institutions in Ukraine during the first years of our state’s independence is far from being completed and should be continued on a new level.

We all have heard on different occasions that this year was the year of Asia for the World Bank and the IMF. Unfortunately, signs of the crisis are now observed on almost all continents. Compared with the situation in the distant 1930s, international financial organizations give us a chance to avoid a long-lasting world depression. We hope that during the next Annual Meetings, we will remember the world crisis as a twentieth century phenomenon that was not granted access to the new century.

Statement by the Governor of the Fund and Alternate Governor of the Bank for the United Kingdom

Gordon Brown

At this time of great challenge for the global economy, I am grateful to have the opportunity to address this most distinguished gathering of world financial leaders. I would like to start by thanking the staff of the IMF and the World Bank for the excellent organization of these meetings—and I would also like to pass on the thanks of Clare Short, U.K. Governor of the World Bank.

Our challenge is compelling. Never in our economic history have so many depended so much on economic cooperation among the nations of the world. And the leadership of the world's economic powers has not been so important or potentially decisive since the post-World War period of international economic transformation—a time when the IMF and World Bank were born and Dean Acheson spoke of being "present at the creation." We, too, present at the creation of a new interdependent and integrated global economy, must now shape that economy and, through stability and growth, ensure prosperity and opportunity for all.

We must never forget that the path of open trade and open capital markets that we have traveled in the past 30 or 40 years has brought unprecedented growth, greater opportunity, and the prospect of better lives for millions across the world. But there is still massive poverty in a world where millions are denied opportunity, and the new economy has brought greater risks of insecurity as well as new opportunities.

No sensible policymaker wants to turn the clock back to protectionism and insularity. But to move forward, we need vigilant and active governments, acting together through reformed international institutions, to ensure that the prosperity that has been achieved by some can be extended to all. And so we must not weaken support for the IMF and World Bank when the need for surveillance and coordination is pressing, but strengthen them by building the operational rules and institutional architecture for the new global financial system.

The statements from the G-7, the Interim Committee, and the Development Committee over the past few days have all demonstrated our shared determination to turn words and analysis into action. The proposals for action that I will outline are rooted in an understanding of what has gone wrong and what we must now do together to get the world economy back on track.

The key challenge now is to devise procedures and institutions—nothing less than new international rules of the game—that help deliver greater stability, and prosperity for all our citizens in industrialized and industrializing economies alike.

The Causes of the Current Crisis

Fifty years ago, that earlier generation began by honestly facing conditions in the world of their day. That must be our beginning as well.

The current financial crisis originated in national economic policy mistakes in Asia and a destabilizing lack of transparency. It grew because of their poorly regulated and often distorted financial sectors. It became global because of insufficient supervision and ineffective risk management in the developed country financial markets. It became a crisis because the initial policy responses were more appropriate to overextended public sectors whereas the problem was overexposed private investors. And it has become a human tragedy affecting millions because our social policy approach is still deficient.

Five weaknesses underlie the crisis—in economic and financial policies, underdeveloped financial sectors in emerging markets, ineffective supervision, poor crisis management, and unacceptably poor social protection. But together they expose an even more fundamental common problem.

For the past 50 years, our policies for regulation, supervision, and crisis management have been devised for what were essentially independent, relatively sheltered national economies with discrete national capital markets and limited and slow-moving international capital flows.

Now that we are in an era of interdependent and instantaneous capital markets, individual economies can no longer shelter themselves from massive, fast-moving, and sometimes destabilizing global financial flows, and it is obvious that if we are to respond to this, we need urgent action now both to sustain domestic demand and make urgent progress for reform at both national and global levels.

Restoring Stability and Growth

First, regarding the current situation, what began last year as a local and regional crisis centered in a handful of Asian countries, with its effects most sharply felt in Asia, has spread from Asia to Europe and South and North America becoming what is now a global problem affecting us all.

Better risk management in the future will lead to more stable capital flows. But it is a matter of concern that many emerging market economies are being caught up in the turmoil, regardless of the strength of their macroeconomic fundamentals. Which is why, as last weekend's G-7 statement has made clear, the G-7 countries—North America, Europe, and Japan—as well as the IMF and the World Bank, stand ready to support all emerging market countries that are prepared to embark on strong sound policies that will involve structural reform. But when the balance of risks in the world economy has shifted from inflation to slower growth, the G-7 countries must now assume greater responsibility.

The necessary improvement in trade balances in affected countries could come either from domestic stagnation or from export-led growth. It is in our shared interests to achieve this export-led growth, but this will only be possible if, by sustaining world demand, the industrialized world is the driving force for that growth. As I said in Japan recently, all industrialized countries must now bear their fair share of the burden of adjustment. No one country can either escape its responsibility or be required to bear the whole burden with all the risks of protectionist sentiment that this would entail. Burden sharing, rather than burden shifting, is the way forward. And I was reassured that, in the recent G-7 statement, members from each respective continent have resolved to play our rightful role and take action to ensure that our economies can both sustain growth and remain open to trade:

- The recent action of the U.S. Federal Reserve in cutting interest rates was designed to sustain domestic demand growth. I was pleased to hear President Clinton say this morning that maintaining free trade, free from protectionism, is an important element of the U.S. response. I know also that the administration is working very hard to ensure ratification of the NAB and the IMF quota increase. We should support and encourage them to step up their efforts in these areas.
- I know, too, from my recent visit to Japan that my Japanese colleagues are focused on their efforts to stimulate domestic demand through fiscal and monetary policy. And, to help restore market and consumer confidence, the Japanese government must make available public funds and lay out a clear timetable for action to restore health to the banks and the financial sector.
- And in Europe too, including the United Kingdom, we will be working to ensure that the euro promotes stability and growth. And the European contribution will include a commitment to employment creation within a policy of structural reform.

Last year, I told this meeting that I was determined to get the British economy back on track for sustained growth with low inflation. That required a necessary slowing in economic growth. The U.K. economy grew last year by 3.5 percent. At the time of our March budget, we expected growth to slow to 2 percent to 2.5 percent in 1998 and 1.75 percent to 2.25 percent in 1999 before returning to trend. So far this year, the latest indications are that we will meet our growth forecast for this year. Six months ago the IMF was forecasting world growth at 3.7 percent in 1999. The turmoil in emerging markets together with the deteriorating economic situation in industrialized countries has led the Fund to revise down expected world growth to 2.5 percent next year. So, with Japan and one-fourth of the world in recession, every country will be affected by the instability that is currently affecting the world economy.

With the IMF forecasting that growth in world trade will fall by two-thirds this year, Britain's export markets are set to grow much more slowly. U.K. exports to Indonesia and Malaysia are already down 50 percent this year; they are down 55 percent to South Korea and down 60 percent to Thailand and the Philippines. Slower world growth makes it inevitable that growth in Britain next year will be more moderate. But as a result of the tough and decisive action this government has taken, Britain is better placed to steer a course of stability in an uncertain and unstable world as we get the British economy back on track for sustained growth. Our first task when we came into government was to set in place a long-term and credible platform to achieve the stability that is an essential precondition for long-term investment, growth, and jobs. It is in pursuit of our long-term goals—high and stable levels of growth and employment—and the rejection of the "short-termism" and stop-go policies that have undermined the U.K. economy in the past—that we have taken tough decisions.

In the face of rising inflationary pressure and the large structural deficit we inherited, we made the Bank of England independent, raised interest rates, and tightened fiscal policy by 20 billion pounds over the past year, amounting to 3.5 percent of GDP from financial year 1996/97 to financial year 1999/2000. Our Pre-Budget Report will set out the next steps, building on this platform of stability, that we must take over the coming year to equip the British economy so that it is more than equal to the challenges that the new global economy brings. Britain cannot be properly equipped while we have productivity levels 40 percent below America, and 20 percent below France and Germany, so over the next year, in partnership with industry, we intend to examine and begin the task of dismantling every barrier to productivity, prosperity, and employment creation. That will require policies to promote entrepreneurship and small business development, to invest in science and innovation, to encourage industrial investment to modernize our infrastructure, and to open all sectors of our economy to greater competition.

In the modern economy, the economies that succeed will be those that get the most out of their people. So, we will continue our reforms to promote greater employability of the British workforce through our New Deals for the unemployed and to make work pay by combining our new Working Families Tax Credit and national insurance reform with the minimum wage. By building upon a platform of stability with our continuing commitment to a stable monetary framework and sound public finances, and united in our determination to promote and sustain domestic demand growth, I can assure you that, at this time of world economic instability, the British government will continue to pursue policies for open trade, investment in productivity, and employment opportunity for all.

Reforming the Financial Architecture

Vigilance in national economic policies today must be matched by a willingness to reform the international financial system to secure greater stability tomorrow. As British Prime Minister Tony Blair said in New York two weeks ago, we must create a new global framework which will have to mirror, at a global level, national regimes for transparency, supervision, crisis management, and stability.

For too long, the financial architecture has been defined in terms of the roles and responsibilities of the international institutions. In fact, the new financial architecture we propose—codes of conduct, the new global regulator, and an international memorandum of understanding—is not about new institutions, but about how, in an interdependent world, we monitor and discipline ourselves and reach decisions in a more coordinated way. The key challenge is to devise new international rules of the game that, by boosting credibility and investor confidence, help deliver stability and prosperity. Our task is not to weaken support for the IMF and World Bank at a time when the need for surveillance and coordination across the world is more pressing, but to strengthen them by building the operational rules and architecture for the new global financial system.

So what are the new "rules of the game" and what are the institutional changes we need? We need to promote greater openness and transparency in national policymaking. In this new world, national governments must set clear, long-term policy objectives that build confidence and commit to openness in policymaking that keeps markets properly informed and ensures that objectives and institutions are seen to be credible.

The way for them to do this is to agree to abide by well-understood, internationally endorsed codes of conduct: for fiscal policy, monetary and financial policy, corporate standards, and social policy. The IMF has already drawn up a code of good conduct for fiscal policy and is now drawing up a code for monetary and financial policy. The OECD is drawing up the corporate code, and the World Bank is considering a social code. Together, these codes will help produce an environment in which financial markets can operate better. They should reduce the risk of future failures, and mean that when failures do occur, the financial system is robust enough to withstand them. By improving public understanding of why and how decisions are made, and making sure the right long-term policies are in place, they will help build public understanding and support for the policies that deliver economic growth and prosperity. Proper implementation of the codes of conduct should be a condition of IMF and World Bank support. Immediate action to promote transparency in policymaking, financial sector reform, and corporate governance should be key components in any reform program to which the IMF and World Bank agree in coming months.

Of course, in this new role, the IMF must be more publicly accountable. We need a systematic approach to internal and external evaluation of the Fund's own activities, including a new full-time evaluation unit inside the IMF, but reporting directly to the Fund's shareholders, and in public, on its performance. And the Fund and Bank must also work much more closely together, particularly in providing advice on financial policy to emerging markets countries. That is why the joint department of the IMF and World Bank we have proposed is essential to carry out this work.

The four codes of good conduct for policymaking, codes agreed by the international institutions, but accepted by national governments, and the radical institutional changes—a merged World Bank/IMF financial regulation department—are key building blocks in the new financial architecture. But I believe we must now go further and develop new global structures for the global age. The events of recent months have pointed out inadequacies in our understanding of the interrelationships between financial markets and between countries, particularly between developed and emerging market economies, inadequacies in the quality of risk assessment and gaps in the international regulatory system. The Basle Committee has published a comprehensive set of core principles for banking supervision and set up a liaison group and consultation group to monitor their implementation. I also welcome the Basle Committee's work on improving transparency and risk assessment.

But we now need a new coordinating mechanism to ensure proper standards and provide regular and timely international surveillance of all countries' financial systems and of international capital flows, not just to point out weaknesses, but to ensure these weaknesses are addressed and to identify systemic risks to the global financial structure. That is why we must examine the scope for a new permanent Standing Committee for Global Financial Regulation, bringing together not only the Fund and Bank, but also the Basle Committee and other regulatory groupings on a regular—perhaps monthly—basis. This global regulator would be charged with developing and implementing a mechanism to ensure that the necessary international standards for financial regulation and supervision are put in place and properly coordinated.

This Standing Committee could also play an important role in strengthening the incentives to the private sector to improve its risk assessment. Recent events have shown that it is particularly important that we have greater transparency of hedge funds, which, wherever they are formally registered, can have an impact on global financial markets. We also need to consider strengthening prudential regulation in both emerging and industrialized countries and particularly for cross-border activities.

Third, the Standing Committee could also help to find better ways to identify systemic risk. In the United Kingdom last year, we published a memorandum of understanding, setting clear divisions of responsibilities and establishing a regular system of meetings and surveillance to ensure cooperation between our national financial institutions to identify and address systemic risk at an early stage. Systemic risk is not confined to national boundaries. What we need is an international memorandum of understanding that would establish the proper division of responsibility at the international level, to reduce the chance of crises occurring.

The IMF should remain at the center of this framework, as part of the new Standing Committee, to coordinate the identification of systemic risk. We need to have clearly defined procedures for deciding when and how to provide liquidity support, without offering a guarantee to private investors that would compound moral hazard. I would like to see the IMF indicate that in the event of a crisis, and where a country adopts good policies, it may be prepared to sanction temporary debt standstills, by lending into arrears, in order to enable countries to reach agreements with creditors on debt rescheduling. By making this clear in advance, private lenders would know that in future crises, they would be expected to contribute to the solution as part of an IMF-led rescue. There also needs to be a better mechanism for the international authorities to liaise with private sector creditors and national authorities to discuss the handling of debt problems at times of potential crisis.

The United Kingdom is also determined to ensure that action is taken at an international level to promote fairness and relieve poverty. We should not allow our discussion of the lessons to be learned from developments in Asia to obscure the important work that is still needed in the poorer countries.

I am pleased that this week, we have agreed on new procedures for advancing debt reduction to post-conflict countries. And to meet our Mauritius Mandate targets, we need to aim for 22 countries to reach the decision point in the HIPC process by the end of 1999. All countries should insist that export credits be used only for productive expenditure. And all countries must stand ready to provide the resources to make progress by 2000.

The responsibility of all of us who lead in the era of globalization is to meet the authentic problems of our times with a vision, an intelligence, and an energy that will make the world economy stronger, more stable, and more prosperous—a world more open, not just to the free flow of goods, but to the rising tide of people’s aspirations everywhere. Globalization has happened—we must now make it work in hard times as well as in good.

The challenges that arise from our ever greater interdependence in an integrated global economy are challenges that summon forth new solutions. So, let us resolve from here in Washington today to do whatever is necessary to create the conditions for stability and growth and to put in place the financial architecture that can achieve the ambitions of 1945 in a new world: to encourage investment flows from private and public sources in even the poorest areas of the world, so that all countries—from the richest to the poorest, most indebted countries—have the chance that they deserve to achieve stability, economic growth, and opportunity for all their citizens.

Statement by the Governor of the Bank for Uzbekistan

Bakhtiar Sultanovich Khamidov

A year has passed since the last Annual Meetings—a year that was marked by a number of important events revealing serious problems at the present stage of global economic development. Recent events provide a basis for serious reflection and examination of the causes and depth of current problems and their spread to the global economy, and for a search for possible ways to solve them.

The consequences of the crisis in a number of countries have demonstrated to the world community the way in which destabilization in a single country may create a wave that spreads crises among diverse regions of the world. This shows that economies cannot exist separately from one another today. At the same time, countries are largely left to their own devices when it comes to resolving their crises.

We must recognize that, in our modern world with all its polarities, there can be no one model for making the transition to a market economy that can be applied to all countries as a universal recipe for reform. The crisis in Southeast Asia and especially in Russia demonstrates that a mechanical duplication of familiar models for market reforms that does not take into account the historical, national, and economic realities of the country will not always produce the expected results; on the contrary, at times it will lead to deep economic crisis and the impoverishment of the people.

I have no doubt that the International Monetary Fund is carrying out an in-depth analysis of the crises that have occurred and is pondering how correct and justified its recommendations in those countries turned out to be. In our opinion, when Fund recommendations are developed and its programs for market reforms are carried out, the specific features of the country and its social mentality, living standard, and initial capacity should be taken into account. The government should be aware of all its risk and responsibility for the consequences of the reform to be carried out. For this, there must be a strong administration and effective government authorities that will be able to preserve political and economic stability and prevent a fall in the public's confidence in the reforms, as has happened in a number of countries. As a rule, when implementing a reform policy, the greatest progress is achieved by those states where the government enjoys the support of a public that understands the reforms and recognizes that they are aimed at raising the living standard.

This approach is of special importance when it is a question of the countries in the post-Soviet area, where the problem of transition from old principles and stereotypes to market principles has turned out to be far more difficult than was expected. This is the result of a need for deep comprehension and understanding of the fact that for more than 70 years these countries were under the influence of an administrative, command-oriented ideology based on principles of totalitarianism. Furthermore, when recommending this or that model for transition from a planned economy to a market economy, many international experts only have a largely theoretical knowledge of planned economies and underestimate the depth of the processes taking place and the possible consequences during the transition period. The experience of a number of countries shows that the implementation of forced systemic and structural reforms in countries with transition economies often leads to social opposition and gives rise to serious economic, religious, ethnic, and other conflicts that impede the introduction of market reforms. It is obvious today that shock therapy is not always a justified means for achieving economic stabilization in the transition economies. There exist successful cases of a number of countries that have chosen their own path of gradual and consistent development. In our opinion, there should be a multitude of ways to make the transition to market conditions, and they deserve the most intent study.

After Uzbekistan acquired its independence, our first aspirations were to reconcile everything valuable and positive from the history of development of the global economic system with those conditions existing at that time in a country which was completely dependent economically on the central authorities and which had the poorest initial potential of the countries of the former Soviet Union. As a result of consistent measures taken by the government of Uzbekistan to develop and deepen its economic reforms, Uzbekistan has today already passed through the critical stage of instability and reached the state of economic growth.

The proof of this is a dynamically growing rate of increase in industrial output and extraction of oil, gas, gold, and nonferrous metals (Uzbekistan has joined the world's top 10 countries in production of these commodities), as well as a growing positive foreign trade balance, which cannot be said of the majority of countries in the transition stage. Our steadily growing GDP is outpacing the increase in the Republic's population. And the growth in industrial production is accompanied by an improvement in the structure of production.

Positive changes in volumes and sources of funding for capital investments are taking place under the influence of our structural reforms.

As a result of the implementation of sound monetary policy, in 1998 inflation declined by a factor of 2.3 compared to the same period last year and comprised 1.5 percent per month. The revenue growth rate exceeded that of expenditures, reducing the budget deficit to 1.3 percent of GDP.

As opposed to many countries experiencing problems servicing external debt, Uzbekistan has pursued a sound external debt policy. We avoid short-term loans to support the balance of payments and attract loans only for project financing. This policy helps keep external debt at a moderate level (about 17 percent of GDP).

Special features in the development of Uzbekistan's banking and financial sector presently consist of the reinforcement and further development of positive tendencies in the areas of monetary circulation and inflation, and stable functioning of the banking system.

The central bank's conservative, strict approach to controlling the country's banking system operations is based on a fundamental principle for implementation of banking sector reform in Uzbekistan—ensuring stability. A decree of the President of the Republic of Uzbekistan on a restructuring of the Republic's banking system which was signed a few days ago serves as proof of this. It permits joint-stock commercial banks to sell up to 50 percent of their stock shares to nonresidents.

I also would like to note the great amount of assistance provided by international financial and economic institutions—the IMF, the World Bank, the IFC, the European Bank for Reconstruction and Development, the Asian Development Bank, and others—in implementing economic reforms and integrating Uzbekistan into the global community. We have now reached that stage of mutual cooperation where we have discovered common priorities and defined areas for further interaction that take into consideration the special features distinguishing Uzbekistan from the other transition economies, insofar as Uzbekistan has chosen its own path for development corresponding to its geopolitical and demographic influence in the region, and that take into account the tradition and mentality of the Uzbek people.

The government of Uzbekistan has worked out a strategy aimed at maintaining financial stability; expanding privatization; deepening reform in agriculture, the banking sector, and small- and medium-scale businesses, and improving the country's export potential, with a view to signing Article VIII of the IMF's Articles of Agreement in 2000.

We believe that, at the present stage of global economic development, the expanded participation of all countries in economic programs involving international institutions and organizations should be viewed as a powerful factor for economic and social stability of individual regions and, as a whole, on the scale of the entire world. I trust that the Bretton Woods institutions will intensify their contribution to the strengthening of that process.

Statement by the Governor of the Fund for Vietnam

Nguyen Tan Dung

Today I am very pleased to represent the government of the Socialist Republic of Vietnam and the State Bank of Vietnam in addressing this meeting of the Board of Governors of the World Bank and the International Monetary Fund.

First of all, I would like to convey the warmest greetings of the government of the Socialist Republic of Vietnam to the Chairman, His Excellency Michel Camdessus, His Excellency James Wolfensohn, Governors, and all delegates of member countries and the appreciation of our government for your contributions to the development of these two most important international financial institutions and your assistance to Vietnam's economic reform and development.

We are meeting here against the background of the increasingly complicated financial crisis in many Asian countries as it spreads geographically and threatens to prolong. And the global credit exhaustion is disrupting the stable development of many countries in and outside the region, forcing the world financial community and countries to face the biggest challenge in recent decades.

Over the past year, despite the tremendous efforts of the governments of the countries facing crisis and the strong support of the World Bank and the International Monetary Fund, there are no clear signs of improvement in major economic indicators of those countries. This situation makes the role of the Bank and the Fund larger and their responsibilities heavier.

I hope that this meeting will devise additional appropriate solutions on the basis of a global coordination of efforts to help countries in crisis improve their situation, prevent recession, quickly recover, and grow. There must be in place effective solutions to assist other countries in containing the risk posed by the contagious affects of the crisis for common benefit of the international community.

As a country in Southeast Asia, Vietnam continues to suffer from the heavy impact of the regional crisis. In addition, Vietnam is also enduring the serious consequences of natural calamities. In 1998, GDP growth is about 6 percent, the lowest level in the last seven years; exports failed to increase substantially; foreign direct investment only reached 60 percent of the 1997 level; unemployment rose; balance of payment difficulties were encountered. The government of Vietnam is watching closely the evolution of the crisis and is drawing valuable lessons from the crisis countries. We believe that given the trend toward interdependence prevailing in the global economy today, a sound macroeconomic policy that maximizes realization of the potential of the domestic economy, in conjunction with taking full advantage of capital flows, is a fundamental condition of sustainable development.

Since 1997, despite many difficulties, the government of Vietnam has consistently continued to accelerate the process of reform with orientation toward a market economy; open the economy for integration into the region and the globe; adjust investment structure; restructure state-owned enterprises and the fields of public finance, banking, trade, and taxation; and closely combine economic and administrative reform to increase the efficiency and competitiveness of the economy. At the same time, we attach special importance to the implementation of programs for the development of agriculture and rural areas, malnutrition elimination, poverty alleviation, and social equality.

However, being a poor and least-developed country, what we have achieved using the resources of our domestic economy and the limited assistance of donors and foreign investors has not been sufficient to prevent the decline in economic growth and the increase in difficulties created by the adverse impact of the regional crisis on Vietnam's economy.

The government of Vietnam is committed to accelerate the reform process at an appropriate pace coupled with structural economic adjustment so that all domestic resources can be maximized, the impact of the crisis can be minimized and socioeconomic stability and development can be maintained. At the same time, we realize that the assistance of the governments of other countries and international financial institutions, especially the World Bank and the International Monetary Fund, will be critical in supplementing our own resources.

We request the Fund and the Bank to increase concessionary funding and to provide technical assistance to Vietnam in a more timely and more practical fashion in implementing economic reform and structural adjustment. And the first thing is reaching agreement on a Structural Adjustment Credit and an ESAF program as soon as possible.

Given the trend of regionalization and globalization of the economy, the effort of each country is the decisive factor, but they are not sufficient to prevent or limit the negative impact of the external crisis, especially for countries at low levels of development. There must be in place a coordination of global efforts to restructure and make the international financial system safer and more effective, decrease the risk of speculative attacks on currencies, establish an early-crisis-warning system and a fast and effective crisis-resolution mechanism.

One lesson of the current crisis is that the liberalization of trade and investment must be consistent with the level of socioeconomic development of each country and its capability to manage its financial system. Therefore, I believe that external advice and assistance must take into account the positive impact of globalization while minimizing the negative effects for the economy of each country.

Finally, I would like to mention the enhancement of the financial resources of the Bank and the Fund to meet the urgent needs of programs relating to crisis resolution, structural adjustments, and assistance to poor countries. Therefore, we need to urgently complete the Eleventh General Quota Review and the IDA fund contributions, as well as allocate additional SDRs to the Fund. I appeal to industrialized countries to continue their strong support for the increase in the financial resources of the Bank and the Fund while cooperating, and coordinating closely with the IMF and the Bank to help countries overcome the crisis, stabilize, and develop.