International Monetary and Financial Committee

Tenth Meeting
October 2, 2004

Statement by Mr. Al-Suwaidi

Statement by His Excellency
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Governor of the United Arab Emirates Central Bank

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First allow me to extend our constituency's congratulations to Mr. Rodrigo de Rato on the occasion of his election as Managing Director of the IMF. We are confident that the Fund will benefit from Mr. de Rato's wide experience, capabilities, and qualities. We would also like to express our thanks to Mr. Horst Köhler for his stewardship of the institution during a turbulent time for the world economy. We wish him all the best in his new presidential position.

Global Economic and Financial Markets Developments and Prospects

It is heartening that the global economic recovery has been accelerating at a pace that has exceeded most observers' expectations, as growth has recently surpassed the historical trend and was widely distributed across the globe. This performance has been spearheaded by a broad-based and solid recovery in the U.S., which is in sharp contrast with the short-lived growth spurts that characterized the recessionary years that began in 2000 despite the exceptionally high dose of expansionary financial policies. Other major industrial countries also contributed in a meaningful way to the buoyancy of the recovery. The Japanese economy, following a decade of recessionary conditions, is rebounding markedly. European growth rates, while less pronounced than those of the U.S. and Japan, are nonetheless encouraging. A number of Asian countries, notably China and India, continue to experience solid expansion. This favorable global environment, as well as the noticeable progress in the implementation of economic reforms, have contributed to a strengthening in most developing countries' economies, including those in the Middle East, Latin America, and Africa. It is well to note that these developments were accompanied, for the most part, by low inflation and financial stability.

Following this relatively quiet and crisis-free period, the international community should not lapse into complacency and underestimate potential risks. There are at least four key risks that could adversely impact global growth and financial stability. For the most part, these risks emanate from the persistent and growing imbalances in the global economy, which are reflected in both the fiscal and current account positions of the major economic regions. The manner in which these imbalances are resolved will resonate throughout the global economy. An important risk is associated with the global transition to higher interest rates as the current growth momentum continues, and the impact of this transition on emerging markets capital flows and debt sustainability. A second risk arises from the change in the structure of the capital inflows financing the U.S. external current account deficit. The decline in the share of equity and foreign direct investment and the increase in the share of

U.S. treasury papers and the inevitable slowdown of dollar-denominated reserves accumulation by central banks in a number of emerging markets economies point to potential vulnerabilities. Finally, the demand-driven increase in oil prices, in spite of record supplies, has been fed by speculative activities that have maintained prices at high levels. In response to this situation, oil exporting countries in the Middle East are producing near full capacity.

The current account imbalances we referred to are global in nature and call for an effective solution based on a cooperative and coordinated set of policies. Policy makers around the world should push through with clearly identified fiscal and structural reforms and the Fund should play a leading role in promoting and coordinating the necessary global effort to resolve these imbalances. In the U.S., the withdrawal of stimulus needs to be carefully managed in order to minimize the risk of shocks in foreign exchange and financial markets, both in the U.S. and the rest of the world. In this connection, we welcome the careful and gradual reversal of the accommodative monetary policy over the past months. While modest and gradual tightening appears to still be the best strategy for the period ahead, the task of determining the optimal pace of tightening is complex, given the uncertainties surrounding the strength of the recovery and the emerging concerns about inflation. In the meantime, it would be important to formulate a concrete medium-term fiscal consolidation plan to eliminate the high budget deficit. A credible fiscal plan would also contribute to the attainment of the Federal Reserve's objective of a measured and gradual increase in interest rates. In a number of European countries, growth has been spurred by the export sector, while domestic demand has been relatively weak. This is not a sustainable situation. There is a clear need to rebalance demand, thereby contributing to an orderly resolution of the global imbalances. The Japanese economy would also benefit from similar rebalancing of demand, as well as accelerating structural reforms aimed at reducing the very high public debt and restructuring regional banks. Emerging market and developing economies should take advantage of the current favorable external conditions to reduce vulnerabilities by restructuring their debt and, where necessary, strengthening their public finances as well as promoting reforms conducive to sustained growth.

IMF Surveillance and Crisis Prevention and Resolution

The increasingly interdependent global economy has added greater importance to Fund surveillance. To safeguard the moral authority of the Fund, surveillance must be administered in an even-handed manner and applied equally to every member of the institution. In addition, there remains scope to further focus surveillance and reduce the coverage of non-core areas, which have been overburdening the institution. One of the areas that would benefit from increased focus in Article IV consultations is the global impact of policies in systemically important economies. At the same time, surveillance of smaller countries would benefit from better linkages of their economic performance and outlook to regional and global developments.

Over the past two or three years, the Fund has introduced a number of new diagnostic tools that are extremely useful in identifying and addressing crises before they occur. The more important ones in our view are the Financial Sector Assessment Program, the Standards and Codes Initiative, and a much-improved debt sustainability analysis. We are of the strong view that the Fund should accord higher priority to further deepening and sharpening these tools and providing technical assistance to the membership, rather than develop new tools at this time.

Early identification of vulnerabilities should lead to initiating corrective actions by the concerned member, preventing the onset of a crisis. However, identifying and addressing a vulnerability are two separate issues. Taking the necessary actions to remedy potential vulnerabilities remains the responsibility of the individual country. In this regard, the Fund should continue to strive to strengthen its dialogue with its members as a trusted advisor. Every effort should be made to safeguard the candor of the discussions.

There is also a need to enhance the design of Fund-supported programs by continuing to streamline conditionality, taking into account country-specific circumstances, and strengthening local ownership of the reform programs. To this end, policy discussions with member countries should always strive to look at alternative options to attain a certain objective. In addition, more emphasis should be accorded to the "quality" of fiscal adjustment, as opposed to only focusing on the "quantity" of this adjustment, in order to ensure its sustainability and to maintain that reforms are growth oriented. In this connection, we welcome and encourage the expansion of the scope and country coverage of the work on the treatment of public investment and, more generally, the design of fiscal policy in surveillance and Fund programs.

Precautionary arrangements are a useful instrument that serves to signal policy soundness and to provide contingency financing. The latter objective is an essential insurance for countries that are undergoing substantial reforms. We look forward to further discussions on the possible use of these arrangements in exceptional access cases. In addition to these arrangements, the Fund has an array of non-financial signaling instruments that can be adapted to different circumstances. This flexibility is appropriate and should be retained. In this connection, we find the proposal to create a non-financial "Policy Monitoring Arrangement", which includes upper credit tranche conditionality without Fund financing, to involve undue rigidity and conditions that are paradoxically tighter than the financing arrangements, particularly with regard to the timing of the completion of reviews and mandatory publication of staff reports. It is not clear to us that a new instrument is needed in view of the existing signaling instruments. Furthermore, this increased pressure on the Fund's members is not conducive to a closer relationship between them and the institution. Let us not put in place a new instrument of dubious need and not likely to be in demand by the membership.

The provision of technical assistance to the membership is an integral part in the effort to support the reduction of vulnerabilities and the implementation of reforms. It is, therefore, important to devote more resources to satisfy the high demand for technical assistance. In this connection, we very much welcome the establishment of the Middle East Technical Assistance Center (METAC), and look forward to the important role it will play in the provision of technical assistance to the region.

As we have emphasized in past meetings, it is imperative to continue to strengthen governance in the Fund, including by enhancing the voice and representation of developing countries, with a view to improving the global ownership and legitimacy of the institution and its policy recommendations. The membership has regrettably made insignificant progress in this area. In addition, the Fund should continue to work within a cooperative approach. This approach has served the membership well and is essential to further enhance the candor of the discussions with country authorities and secure their collaboration, thus contributing to the effectiveness of surveillance. Improving the diversity of Fund staff would also contribute to the quality of its work and its legitimacy. Here, I would like to point to the fact that the Middle East, and especially the Arab region, is by far the most under-represented area among Fund staff, both in general and in the most senior positions, and call on the management of the institution to give priority to addressing this unsatisfactory situation.

For many years, the membership has called on the industrial countries to liberalize their trade policies to permit increased market access for developing countries. The initial framework agreement reached at the last round of the WTO meeting on reducing subsidies is an important development in this regard. We look forward to a speedy implementation of this initiative and hope that further measures to liberalize trade will be pursued actively, thereby laying the ground work for further needed progress. We encourage the Fund to continue to increase its role in promoting these reforms in the context of surveillance, including of major industrial countries. In addition, priority should be given to the provision of technical assistance and, as appropriate, financial assistance through the Trade Integration Mechanism to developing countries in support of their trade liberalization efforts and to mitigate the short-term costs and risks.

Looking forward, there has been a recent discussion in the Board about the strategic direction of the Fund. This is a very complex subject that is of great importance. The Board discussion was, however, hurried with no time for preparation and deliberation. The rush for action is not in the best interest of the institution or the membership. We believe that this topic should be prepared for, and considered by the Board very carefully, and thus do not believe that targeting a report on it by next Spring is appropriate. We also would like to underscore the agreed practice that all issues that are presented to the IMFC are first discussed by the Executive Board before they are taken up by the IMFC Deputies.

The Role of the Fund in Low-Income Countries (LICs)

The Fund's support of nationally-led efforts to achieve macroeconomic stability through policy advice, financial support, and technical assistance continues to be a key factor in promoting growth, poverty reduction, and the achievement of the Millennium Development Goals in low-income countries. We support the thrust of the *Statement on the Role of the Fund in Low-Income Countries*, which strikes the right balance between the need for the institution to take on its responsibility in helping LICs in their development efforts, and the importance of keeping the Fund's involvement within the confines of the institution's core mandate. With regard to policy advice, the Fund should direct its effort to help countries identify their particular sources of growth and to assess the poverty and social impact of macroeconomic policies in the context of program design and surveillance. Provision of technical assistance and more engagement with country authorities should be at the heart of the effort to build LICs' capacity to design, implement, and monitor macroeconomic policies. Notwithstanding the progress achieved in recent years, the deep-rooted problems of LICs, which underlie their macroeconomic difficulties, suggest that they are likely to be long term users of Fund concessional resources. The Fund should be prepared to respond to this need.

We welcome the progress in the implementation of the Enhanced HIPC Initiative and underscore the potential need for mobilizing additional resources for the three protracted arrears cases that are likely to join the Initiative. The recent modification to the Poverty Reduction Strategy Paper Approach is rightly aimed at better aligning it with domestic processes and institutions, and strengthening countries' ownership of the process. For the period ahead, we are hopeful that the focus of the approach will shift from process application to effective implementation.

The international community should also strive to increase the level of development assistance to help LICs reach the Millennium Development Goals. In this regard, while emphasis should remain on meeting the U.N aid target, there is merit in further investigating the details of the International Finance Facility proposed to bring forward aid pledges and smooth out disbursements. In this regard, it is important to guard against further complicating the modalities and conditionality associated with aid delivery, ensure that disbursement are consistent with the ability of countries to absorb aid and/or their need to enhance capacity, and ensure that the Facility does not lead to a serious drop in ODA once it expires.

The Debt Sustainability Framework under consideration represents a good advancement in the Fund's understanding of the complex debt sustainability issues in LICs. By incorporating countries specific characteristics, it represents an adequate basis to inform the Fund's judgment on debt sustainability.

As we have emphasized in the past, we are of the firm view that the success of the ongoing efforts to eradicate poverty while maintaining macro stability in LICs depends to an important extent on the ability of countries to improve their export performance. The promotion of trade liberalization in industrial countries should continue to top the Fund's agenda to enhance growth opportunities in LICs and the rest of the world.

Developments in the Arab Region and the Role of the Fund

Growth strengthened over the past year in both non oil and oil-exporting Arab countries despite the continued geopolitical tension in the region. Inflation remained low, and both the fiscal and external current account balances improved in most of these countries. In addition, gross official reserves increased, external debt declined, bond spreads narrowed, and financial sector indicators strengthened. This favorable performance was underpinned by prudent financial policies as well as the progress made in structural reforms aimed at strengthening budget and expenditure management and improving the underlying fiscal situation, enhancing the financial sector's supervisory and regulatory framework, and encouraging private investment. Notable progress is also being made in trade liberalization, including in the context of both bilateral and multilateral trade agreements. While the region's economic outlook will remain to a large degree dependent on oil prices and security developments, the non-oil sectors have benefited from the wide-ranging reform efforts and are poised to benefit from the improved global environment. The countries of the region are determined to continue their reform efforts, with a view to raising growth and creating job opportunities for their fast growing population. These efforts will require continued technical and, in some instances, financial support in view of the magnitude of the reform agenda and the uncertainty created by the geopolitical tension and difficult security situation in some countries.

I would particularly point to the difficult humanitarian and economic conditions in Iraq and Palestine. The international community should spare no effort to promote peace and security in these two countries and to end the suffering of their people. We welcome the central role of the Fund in the provision of technical assistance to the two countries and in coordinating donor financial support, and look forward to the institution's increased direct involvement in Iraq.