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Statement by the Hon. **ZVI ECKSTEIN,**
Alternate Governor of the Fund for **ISRAEL,**
at the Joint Annual Discussion

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Mr.Chairman, distinguished Governors, Mr. Dominique Strauss-Kahn, Managing Director of the International Monetary Fund, Mr. Robert Zoellick, President of the World Bank Group, delegation members, ladies and gentleman:

Unfortunately, Governor Stanley Fischer could not be present here. It is a special pleasure for me to be here today to deliver this address on his behalf, and on behalf of the State of Israel.

I would like to make brief comments on two issues: first, the Israeli economy; second, the Fund's Reforms and Policy Agenda. The limited time available will not allow me to cover other important topics, including global economic developments, especially in light of financial market turbulence, the implication of the current energy and food prices on the poorer countries and communities that are not endowed with such resources, and other important issues such as climate change.

1. **The Israeli economy**

Since 2004 and up to the first quarter of 2008, the Israeli economy has been growing at an average annual rate of more than 5 percent. In the second quarter of 2008, GDP growth decreased to approximately 4 percent. Given financial turbulence, global slowdown, and the strengthening of the Shekel, further slowdown is expected in the remaining part of the year and in 2009.

The Israeli economy is effected, like the rest of the world – by the substantial increase in uncertainty in the global financial markets. In Israel, the economy, in general, and the financial sector, in particular, are in good condition in order to address the possible ramifications of the crisis. Relative to banks in the US and in Europe, the Israeli banking sector is conservative and its exposure to the financial turmoil in the US and Europe is limited. I will briefly review recent macro-economic developments in Israel.

In 2008, mostly as a result of significant increases in energy and food prices in the first half of the year, inflation is expected be above the target range (1-3 percent per annum), but inflationary expectations for the next 12 months are within the target range and inflation is likely to return to the target range in the second quarter of 2009.

The balance of payments is expected to be in 2008 in a surplus of around 1 percent of GDP. Controls on capital flows have been removed progressively since the early 1990's, and the capital account is essentially totally liberalized.

On March 24, 2008, the Bank of Israel announced a plan to increase its foreign exchange reserves by purchasing foreign currency in the open market. With effect from 10 July the Bank purchases an average of $100 million a day. This decision was made following an examination of the market conditions and in light of the rapid cumulative appreciation of the shekel.

The government debt ratio is on a declining path, yet it still remains too high and needs to be reduced further; government spending has been consolidated and needs to be further reduced; unemployment went down to 5.9 percent in the second quarter of 2008, and more needs to be done to improve the standard of living of the poorest members of the population.

On May 2007, the OECD Ministerial Council Meeting decided to start the accession process with five countries, including Israel. Following this decision, Israel is now engaged in a dialogue with the organization, and expects to become a full member of the organization in 2010. The process entails updating legislation and adapting to the Organization's advanced standards. It would also serve as an incentive for Israel to continue promoting economic reforms.

At present we are continuing to work on a new and modern central bank law that will clearly define the independence of the Bank of Israel, while increasing its accountability and transparency.

2. The Fund's Reforms and Policy Agenda

The Fund invests substantial energy in reexamining its role, advancing the surveillance agenda, reviewing lending instruments, and strengthening governance. As part of a re-organization, the IMF has cut spending and the number of staff, and highly qualified new professionals have been nominated to senior positions.

First, we welcome the Fund's sharper focus on refocusing its surveillance work. We, as other central banks, have found the Fund's fiscal policy analysis helpful. The overall quality of Fund's surveillance is held in high regards. These days, the obvious demand around the globe is for additional value added in the analysis of the financial sector. Needless to say, the Fund's FSAP work in identifying financial vulnerabilities have had a substantial contribution, but there is value in further work on risk assessment and early warnings. The 2008 Triennial Surveillance Review Paper (prepared by the Fund's Strategy, Policy and Review Department and discussed in the Board on September 26) states that there is a large unmet demand for analysis of financial sector issues, exchange rate analysis and external stability risks, as well as of the of two-way transmission channels between financial and real sectors, and cross border spillover effects. We support the recommendation of the report. It is valuable to increase efforts in developing a framework of a more systematic macro-financial surveillance. In addition, it is important to adopt further steps in order to speed up the completing of Article IV reports and to increase its use of interim reports.

Second, regarding the design of new lending instruments, such as the Rapid Access Line, the Financial Stability Line and the Rapid Liquidity Line, I would like to note that there is indeed value in introducing credit facilities to countries with sound policies, without the traditional conditionality structures. It is desirable that such facilities would be available to increase access to contingent liquidity instruments in order to assist member countries to reduce the risk of capital account crisis and assist those qualifying after being hit by turbulence in global capital markets.

Third, the Fund is an effective international organization that is in the process of improving its governance and accountability. It is important that member countries' authorities will benefit from the continued relevance of the IMF, especially for global financial issues. Such relevance is also tied to the issue of vote and representation. In order to reflect the current global economic situation, new economic powers deserve a bigger weight in the decision making process. With respect to low income countries, the increased desire for vote should be balanced by the implications of increasing the weight of borrowers in any lending financial institution.

Before I conclude, I would like to make another point regarding the global financial crisis and state that during this critical period in the so-far ever-worsening crisis, government policy needs to be guided by two central principles: central banks need to ensure that sufficient liquidity is provided to the banking system and the money and short-term credit markets to ensure their continued effective operation; and governments need to stand ready to inject capital into their banking systems to ensure the stability of the system and the continued provision of credit to the economy.

Thank you Mr. Chairman.