INTER-AMERICAN DEVELOPMENT BANK
INTER-AMERICAN INVESTMENT CORPORATION

PROCEEDINGS

Forty-fifth Annual Meeting of the
Board of Governors of the Bank

Nineteenth Annual Meeting of the
Board of Governors of the Corporation

Lima, Peru
March 2004

FOREWORD

This publication contains the official record of and additional information on the Forty-fifth Annual Meeting of the Board of Governors of the Inter-American Development Bank and the Nineteenth Annual Meeting of the Board of Governors of the Inter-American Investment Corporation, held jointly in Lima, Peru, from March 29–31, 2004. It includes the resolutions approved between the Forty-fourth and Forty-fifth Annual Meetings of the Bank and those approved during the latter of these meetings, as well as the resolutions approved during the Nineteenth Annual Meeting of the Corporation. It also contains the addresses delivered at the meetings and the list of participants, which includes the official delegations, Senior Management and Boards of Executive Directors of the Bank and the Corporation, and observers.

The Forty-fifth Annual Meeting of the Board of Governors of the Inter-American Investment Bank and the Nineteenth Annual Meeting of the Board of Governors of the Inter-American Investment Corporation were held in Lima, Peru, from March 29–31, 2004.

The Inaugural Session opened under the chairmanship of the Temporary Alternate Governor for Italy, Mr. Augusto Zodda. The agendas of the Annual Meetings of the Bank and of the Corporation (see page 3) were then approved, after which the Temporary Alternate Governor for Italy—in his capacity as outgoing Chairman of the Boards of Governors—reported on work performed since the previous Annual Meeting. Subsequently, Mr. Pedro Pablo Kuczynski, Governor for Peru, was elected Chairman of the Boards of Governors.

The Inaugural Session was attended by Mr. Oscar Luis Castañeda Lossio, Mayor of Lima, His Excellency Alejandro Toledo, President of the Republic of Peru, Mr. César Gaviria, Secretary General of the Organization of American States, and Mr. José Luis Machinea, Executive Secretary of the Economic Commission for Latin America and the Caribbean (ECLAC).

A. Matters considered by the Board of Governors of the Bank

1. Report of the Chairman of the Board of Governors and of the Committee of the Board of Governors on work performed since the previous Annual Meeting

   At the Inaugural Session, the Board of Governors took note of the report of the Chairman of the Committee of the Board of Governors of the Bank on work performed since the previous Annual Meeting. The report appears on page 145.

2. Annual Report of the Bank and financial statements for 2003

   During the Second Plenary Session, the Board of Governors adopted Resolutions AG-1/04, AG-2/04 and AG-3/04, respectively, approving the financial statements of the Ordinary Capital resources, the Fund for Special Operations, and the Intermediate Financing Facility Account, for the fiscal year ending December 31, 2003.

   In addition, pursuant to section 2(b) of Resolution AG-12/83, the Board of Governors allocated to the Intermediate Financing Facility Account an aggregate amount equivalent to US$72.6 million in convertible currencies from the General Reserve of the Fund for Special Operations, as set forth in Resolution AG-2/04.

3. Selection of outside auditors for 2004

   During the Second Plenary Session, the Board of Governors selected Ernst & Young LLP as outside auditors for the Bank, in the terms set forth in Resolution AG-2/04.

4. Sites and dates of future annual meetings of the Boards of Governors of the Bank and the Corporation

During the Fourth Plenary Session, the Board of Governors adopted Resolution AG-5/04, resolving to hold the Forty-seventh Annual Meeting of the Board of Governors in Nassau, The Bahamas, from March 20–22, 2006.

The Board of Governors also adopted Resolution AG-6/04 whereby appreciation was expressed for the invitations extended by the Governors for Panama, Belgium, Costa Rica, and Mexico. The Board of Executive Directors was asked to submit its recommendations in due course concerning the sites and dates of future annual meetings.

B. Matters considered by the Board of Governors of the Corporation

1. Report of the Chairman of the Board of Governors and Chairman of the Committee of the Board of Governors on work performed since the previous Annual Meeting

At the Inaugural Session, the Board of Governors took note of the report of the Chairman of the Committee of the Board of Governors of the Corporation on work performed since the previous Annual Meeting. The report appears on page 147.

2. Annual Report of the Corporation and financial statements for 2003

During the Third Plenary Session, in accordance with Article IV, Section 2(c)(v) of the Agreement Establishing the Corporation, the Board of Governors adopted Resolution CII/AG-1/04, approving the financial statements of the Inter-American Investment Corporation for the financial year ending December 31, 2003, which were part of the Corporation's Annual Report.

Carlos Ferdinand
Secretary of the Bank and of the Corporation

AGENDA OF THE FORTY-FIFTH ANNUAL MEETING OF THE BOARD OF GOVERNORS OF THE INTER-AMERICAN DEVELOPMENT BANK

1. Report of the Chairman of the Board of Governors and of the Committee of the Board of Governors on the work done since the last Annual Meeting

2. Election of the Chairman of the Board of Governors

3. Annual Report of the Bank. Financial statements for 2003:

   – Ordinary Capital

   – Fund for Special Operations

   – Intermediate Financing Facility Account

4. Selection of outside auditors for 2004

5. Site and date of the Forty-seventh Annual Meeting of the Board of Governors

6. Sites and dates of future annual meetings of the Boards of Governors of the Inter-American Development Bank and the Inter-American Investment Corporation

AGENDA OF THE NINETEENTH ANNUAL MEETING OF THE BOARD OF GOVERNORS OF THE INTER-AMERICAN INVESTMENT CORPORATION

1. Report of the Chairman of the Board of Governors and of the Committee of the Board of Governors on the work done since the last Annual Meeting

2. Election of the Chairman of the Board of Governors

3. Annual Report of the Corporation. Financial statements for 2003

RESOLUTION AG-1/04

FINANCIAL STATEMENTS OF THE ORDINARY CAPITAL RESOURCES

WHEREAS:

The outside auditors of the Bank, selected in accordance with Article VIII, Section 2(b)(x), of the Agreement Establishing the Bank, have issued an unqualified opinion on the financial statements of the Bank;

The Board of Governors

RESOLVES:

That the financial statements of the Bank with respect to the Ordinary Capital resources for the fiscal year ended December 31, 2003, containing the general balance sheet and the statement of profit and loss, are approved.

(Adopted March 29, 2004)

RESOLUTION AG-2/04

FINANCIAL STATEMENTS OF THE FUND FOR SPECIAL OPERATIONS

WHEREAS:

The outside auditors of the Bank, selected in accordance with Article VIII, Section 2(b)(x), of the Agreement Establishing the Bank, have issued an unqualified opinion on the financial statements of the Bank; and

Resolutions AG-12/83, AG-3/90 and AG-9/95, and the mandate of the Board of Governors in connection with the funding of the Bank's participation in the HIPC Initiative, prescribe that the Board of Governors shall annually allocate amounts in convertible currencies of the General Reserve of the Fund for Special Operations to the Intermediate Financing Facility Account;

The Board of Governors

RESOLVES:

1. That the financial statements of the Fund for Special Operations for the fiscal year ended December 31, 2003, containing the general balance sheet and the statement of profit and loss, are approved.

2. To allocate to the Intermediate Financing Facility Account an aggregate amount equivalent to US$72,600,000 in convertible currencies of the General Reserve of the Fund for Special Operations.

(Adopted March 29, 2004)

RESOLUTION AG-3/04

FINANCIAL STATEMENTS OF THE INTERMEDIATE FINANCING FACILITY ACCOUNT

WHEREAS:

The outside auditors of the Bank, selected in accordance with Article VIII, Section 2(b)(x), of the Agreement Establishing the Bank, have issued an unqualified opinion on the financial statements of the Bank;

The Board of Governors

RESOLVES:

That the financial statements of the Intermediate Financing Facility Account for the fiscal year ended December 31, 2003, containing the general balance sheet and the statement of changes in fund balance, are approved.

(Adopted March 29, 2004)

RESOLUTION AG-4/04

SELECTION OF OUTSIDE AUDITORS

WHEREAS:

Pursuant to Article VIII, Section 2(b)(x) of the Agreement Establishing the Bank, the Board of Governors has the authority to select outside auditors of the Bank;

Pursuant to Resolution AG-05/03, the Board of Governors selected Ernst & Young LLP to serve as outside auditors of the Bank with respect to the fiscal year 2003;

Pursuant to an agreement between the Bank and Ernst & Young LLP, dated June 17, 2002, and a letter from the Bank to Ernst & Young LLP, dated September 23, 2002, the parties may extend, on a yearly basis through and including the fiscal year 2006, the existing appointment of Ernst & Young LLP as outside auditors of the Bank; and

The Board of Executive Directors has recommended to the Board of Governors that Ernst & Young LLP be selected to serve as outside auditors of the Bank with respect to the fiscal year 2004;

The Board of Governors

RESOLVES:

That, pursuant to Article VIII, Section 2(b)(x) of the Agreement Establishing the Bank, Ernst & Young LLP is selected to serve as outside auditors to certify to the general balance sheet and the statement of profit and loss of the Bank with respect to the fiscal year 2004, in accordance with Section 10 of the By-Laws of the Bank.

(Adopted March 29, 2004)

RESOLUTION AG-5/04

SITE AND DATE OF THE FORTY-SEVENTH ANNUAL MEETING
OF THE BOARD OF GOVERNORS

The Board of Governors

RESOLVES:

To hold the Forty-seventh Annual Meeting of the Board of Governors in Nassau, The Bahamas, from March 20–22, 2006.

(Adopted March 31, 2004)

RESOLUTION AG-6/04

SITES AND DATES OF FUTURE ANNUAL MEETINGS OF THE BOARDS OF
GOVERNORS OF THE INTER-AMERICAN DEVELOPMENT BANK AND
THE INTER-AMERICAN INVESTMENT CORPORATION

WHEREAS:

Prior to the Forty-fifth Annual Meeting of the Board of Governors, the Governors for the following countries offered to host annual meetings of the Boards of Governors of the Bank and the Corporation in the years listed in parentheses: Japan (2005), The Bahamas (2006), Panama (2007), Belgium (2008), Costa Rica, Ecuador and Mexico;

The Board of Governors, pursuant to Resolution AG-6/03, decided to hold the Forty-sixth Annual Meeting of the Board of Governors in Okinawa, Japan; and

The Board of Executive Directors, pursuant to Resolutions AG-1/76 and AG-5/00, decided to submit a proposed resolution to the Board of Governors during the Forty-fifth Annual Meeting, recommending that the Forty-seventh Annual Meeting of the Board of Governors be held in Nassau, The Bahamas;

The Board of Governors

RESOLVES:

1. To express its appreciation for the invitations extended by the Governors for Panama, Belgium, Costa Rica, and Mexico, as well as such other invitations as may be extended during the course of the Forty-fifth Annual Meeting of the Board of Governors.

2. To instruct the Board of Executive Directors, following the procedure approved by means of Resolution AG-1/76 and pursuant to Resolution AG-5/00, to present its recommendations concerning the sites and dates of future annual meetings of the Boards of Governors of the Inter-American Development Bank and the Inter-American Investment Corporation in due course, in accordance with the terms of reference set forth in document AB-476-2.

(Adopted March 31, 2004)

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RESOLUTION CII/AG-1/04

FINANCIAL STATEMENTS OF THE
INTER-AMERICAN INVESTMENT CORPORATION

WHEREAS:

The external auditors of the Corporation, selected in accordance with Article IV, Section 2(c)(vii), of the Agreement Establishing the Corporation, have issued an unqualified opinion on the financial statements of the Corporation;

The Board of Governors

RESOLVES:

That the financial statements of the Corporation with respect to the fiscal year ended December 31, 2003, containing the balance sheet and the statements of income and retained earnings and of cash flow, are approved.

(Adopted March 30, 2004)

Wednesday, March 24

9:00 a.m. to 5:30 p.m.	Registration of participants

Thursday, March 25

8:00 a.m. to 6:30 p.m.	Registration of participants
9:00 a.m. to 5:30 p.m.	Seminar: "Latin American and Caribbean Social Capital in Action: Young Entrepreneurs and Volunteerism"
9:30 a.m. to 1:00 p.m.	Rural Competitiveness Round Table: "Agricultural Technological Innovation in Latin America and the Caribbean: Challenges, Opportunities, and Resources"
3:00 p.m. to 4:30 p.m.	Round Table of the Interagency Group for Rural Development and Ratification of AECI's Accession to the Interagency Group

Friday, March 26

8:00 a.m. to 6:30 p.m.	Registration of participants
9:00 a.m. to 7:30 p.m.	Seminar: "Latin American and Caribbean Social Capital in Action: Young Entrepreneurs and Volunteerism"
9:30 a.m. to 7:00 p.m.	Seminar: "City and Marginality: Strategies for Social, Economic and Spatial Integration"

Saturday, March 27

8:00 a.m. to 6:30 p.m.	Registration of participants
9:30 a.m. to 7:30 p.m.	Seminar: "New Frontiers in State Reform"
10:00 a.m. to 11:30 a.m.	Round Table on Remittances
10:00 a.m. to 6:30 p.m.	Seminar: "Lessons and Perspectives for Infrastructure Investment in Latin America and the Caribbean"
3:00 p.m. to 6:30 p.m.	Preliminary Session of Heads of Delegation to the Annual Meeting of the Boards of Governors of the IDB and IIC, followed by Meetings of the Committees of the Boards of Governors of the IDB and the IIC

Sunday, March 28

8:00 a.m. to 6:30 p.m.	Registration of participants
9:30 a.m. to 1:00 p.m.	Seminar: "Governments and Banks: Responsibilities and Limits"
3:00 p.m. to 6:00 p.m.	Special Governors' Meeting

Monday, March 29

8:00 a.m. to 5:30 p.m.	Registration of participants
9:30 a.m. to 12:30 p.m.	Inaugural Session (First Plenary Session)
3:00 p.m. to 6:30 p.m.	Second Plenary Session

Tuesday, March 30

9:30 a.m. to 1:00 p.m.	Third Plenary Session

Wednesday, March 31

9:30 a.m. to 12:30 p.m.	Fourth Plenary Session and Closing Session

ADDRESS BY MR. AUGUSTO ZODDA, TEMPORARY ALTERNATE GOVERNOR FOR ITALY, ON BEHALF OF THE OUTGOING CHAIRMAN OF THE BOARDS OF GOVERNORS OF THE INTER-AMERICAN DEVELOPMENT BANK AND THE INTER-AMERICAN INVESTMENT CORPORATION

First of all, I would like to thank the Government and the people of Peru—and in particular the city of Lima—for their warm and generous hospitality. I would also like to congratulate the Bank's Management and staff for the excellent arrangements of this Annual Meeting.

It has been a great honor for Italy to chair the Boards of Governors during 2003: a challenging year for the Inter-American Development Bank, and for Latin America and the Caribbean countries.

In this regard, I would like to seize this opportunity to comment briefly on the developments that have characterized the global outlook and the Latin American and Caribbean region, specifically, as well as the accomplishments that the Bank has attained since our last meeting in Milan, one year ago.

The International Scenario and Latin America and the Caribbean

Although sources of uncertainty have not completely disappeared, the international outlook has been improving since the second half of 2003.

Prospects of growth in the United States continue to be robust. Positive signals are coming also from Japan. Recent data show that recovery is gaining some momentum in Europe, too.

Prospects for the Latin America and Caribbean region look positive, underpinned by a strengthening of domestic demand, signs of capital re-flow, and global recovery.

These signals are the clearest evidence that not only the reform process undertaken in the region needs to be maintained, but reforms also need further implementation and progress.

Reform to Promote Growth

We all know that some of the conditions needed to achieve strong and sustainable growth are: prudent macroeconomic policies; the quality of public institutions; healthy financial markets; actions to promote social development; increased productivity and higher income among the poorest layers of the population.

These conditions have now been included in the "New Sector Strategies Package" endorsed by the Board of Executive Directors last year. The new strategies not only signal a new vision in the Bank's operations in the region, but they also will provide guidance for all the stakeholders committed to improve the living conditions and future of the poorest people of Latin America and the Caribbean.

To implement these new strategies, greater efforts must be made by the Bank, the international community at large and the countries themselves—being ultimately responsible for setting up the economic, legal and social framework necessary to pursue a balanced development.

The task is not easy. As it will not be easy for the region to achieve even the first of the Millennium Development Goals that is to reduce extreme poverty in the region by half by 2015. In fact, assuming that no significant change in income distribution occurs, to reach such a target would require an increase of the average per capita growth rate of at least 4 percent per year from the 1.5 percent recorded over the last decade.

Poverty and Inequality

Economic growth, however, is not the only factor to concentrate on. As poverty is multidimensional in nature, various strategies and policies can be pursued to alleviate this plague. To start with, a reduction in the huge income inequality characterizing Latin America—itself a major obstacle to economic growth—is needed.

If in the long run everybody benefits from economic policies triggering growth, it is indeed our duty to take into consideration also the short-run impacts of these policies. We welcome therefore the Bank supported efforts to improve the quality of poverty reduction and equity enhancement policy in the region.

In this respect, an enhanced investment in human capital is a key to success in reducing inequality: it translates into a higher degree of efficiency in human resources and in an improvement of the competitiveness of local firms.

The Private Sector and the IDB Group

As the global economy recovers we must ensure that no country in the Latin American and Caribbean region is left behind. However, various economic surveys show that the general business environment in this area is not satisfactory.

Over the years the Bank Group has devoted considerable resources to improving the investment climate in the area by eliminating regulatory barriers to private sector participation and by boosting competitiveness in the economy.

We have seen a lot of attention in the Bank on this issue. The body of experience developed by the Inter-American Investment Corporation, the Multilateral Investment Fund and by the Bank itself in dealing with private sector development in the region is a real asset. Synergies within the "IDB Group" should be enhanced. We want to thank Minister Kuczynski for the precious work done in this respect by his External Review Group.

On another front, we welcome the support given to the new Strategy, which will guide the IDB Group activities in the private sector in the coming years. Management is now encouraged to promptly start working on the implementation plan. We also note, with satisfaction, the Bank's active role in promoting the "Business Climate Initiative" in order to improve business conditions for the private sector.

Over the years, we have learned that the most dynamic sector of any economy, if adequately supported, is small business. A productive system based on a myriad of firms far from being a constraint to economic growth can be an asset over time. The benefits of this productive system go beyond the mere economic factors. That is to say it can contribute to reduce social inequalities and improve participation in local public institutions.

We restate, therefore, our support to the Bank's commitment of tripling by 2007 its volume of lending operations through the banking system to micro, small, and medium-sized enterprises.

Trade and Finance

During the last decades, significant progress has been made in reducing trade and financial barriers. This represents an important factor in sustaining global growth. The growing interdependence of markets and, especially, the fast movement of capital, has intensified competition over financial resources. As a result, the Latin American countries end up being more vulnerable to competition from other emerging market economies.

This vulnerability is aggravated by a regional environment characterized by high public debt and fragile financial markets.

Recent experience shows that financial crises have had a serious impact on social conditions. Hence, we should be supportive of sound macroeconomic policies aimed at improving countries' resilience to financial crises. This strategy would be beneficial for the social conditions of the area over the long run.

In the same vein, we should support local capital markets development, which contribute to reducing the risk of financial crises by limiting countries' dependency on external borrowing.

Role of the IDB and Development Effectiveness

Sustainable development requires financial and institutional resources. The approval of over US$6.7 billion in new lending operations is a proof of the Bank's continuous commitment to support the development of the region. By diversifying its lending instruments the Bank has been able during the last years to respond timely and efficiently to the borrowing countries' different needs. We welcome in this regard the progress report on the status of the new lending instruments, and the approval of the new capital adequacy framework, aiming at preserving and strengthening the financial soundness of the Bank.

An effective Bank strategy should be supported by an effective aid policy. Following the resolution approved at the 2002 Annual Meeting in Fortaleza, and the indications given by Governors at the 2003 Annual Meeting in Milan, several initiatives have been undertaken by the Bank on development effectiveness. We reiterate the importance of strengthening development effectiveness to help the Bank fulfill its objective of poverty and inequality reduction, as well as to assist the countries in addressing the Millennium Development Goals.

Evidence has shown that resources are more effectively and efficiently used in countries with sound policies, institutions and governance. Therefore, we encourage the Bank to support the Latin American and Caribbean governments in their effort to make the most effective use of resources.

The adoption of a result-oriented approach by the Bank, as well as by the other Multilateral Development Banks, may be at the basis of a virtuous circle where satisfactory results may increase support to raise further the current level of Official Development Assistance.

Internal Governance

Internal governance is a key factor of the IDB Group activity. We welcome the important progress attained by the IDB in the field of transparency and in strengthening good governance. This is of crucial importance, at a time when the whole international financial system is put into question and development aid policy, in particular, is being subjected to intense scrutiny.

The adoption of the new Information Disclosure Policy, for instance, represents a major step forward for the Bank in terms of transparency. It is important that the Bank will continue to follow this path and make every effort to be at the forefront among the multilateral development banks in terms of transparency and accountability.

Conclusion

Fellow Governors, this meeting will provide a fruitful opportunity to express our expectations and wish on the future direction to be taken by the Bank.

I am confident that our dialogue will contribute to the fight against poverty, which is the core priority of this Institution, whilst contributing to the long-term development of the region.

I trust that the Bank, under the wise leadership of President Iglesias, will be well equipped to face the challenges that lie ahead. On behalf of the Board of Governors I would like to express to you, Mr. President, our sincere appreciation for your long and continued commitment to the region.

Let me also seize this opportunity to thank you, Fellow Governors, for your guidance and assistance to the Italian Chairmanships over the last year.

ADDRESS BY MR. PEDRO PABLO KUCZYNSKI, CHAIRMAN OF THE BOARDS OF GOVERNORS OF THE INTER-AMERICAN DEVELOPMENT BANK AND THE INTER-AMERICAN INVESTMENT CORPORATION, AND GOVERNOR FOR PERU

It is an honor and a pleasure for Peru to host this important meeting of the IDB and of the Corporation. Welcome to Peru and to Lima!

We extend our greetings to the Representative of Italy, who chaired last year's meeting in the magnificent city of Milan, as well as to the Representative of Japan, where the meeting will be held next year on the beautiful island of Okinawa.

Economic Conditions and Growth

This meeting takes place at a turning point for the economies of Latin America. After a long period of recession, the region's major economies are returning to growth. Regional GDP is expected to rise by 4.4 percent this year, spearheaded by Chile and the economic recovery in Argentina, Brazil, and Venezuela. By contrast, the regional growth rate was only 1.3 percent in 2003, and near zero in prior years.

The key question now is how to achieve more sustained, predictable growth. Growth may not be the only recipe for reducing the poverty and unemployment that plague most of our countries, but it is a precondition for any reform effort.

The lesson learned from the 1990s, during the euphoria of strong economic growth expectations, was that macroeconomic management, especially as it relates to exchange rates and fiscal and monetary matters, calls for common sense and avoidance of extremes. The huge devaluations necessary in Mexico, Brazil, and later Argentina slowed annual growth in Latin America by one percentage point during the decade of 1991–2001. We grew by only 3 percent, rather than four, despite foreign capital inflows in excess of 4 percent of annual GDP throughout that period. Internal economic and financial imbalances cost the region dearly in recent years. Deteriorating terms of trade were also detrimental.

One key requirement for sustained growth, then, is a viable macroeconomic framework. The other is progress on both "first-generation" and "second-generation" reforms in such areas as education, the judicial system, citizen security, and greater transparency and openness in credit and capital markets. Only with a coherent program of reforms tailored to the particular needs of each country can we hope to usher in a period of more sustained, predictable growth than in the past 25 years.

From 1940 to 1980, Latin America and the Caribbean grew at a steady, even rate of 5.2 percent annually. It was a different world, of course, but we must strive to regain that momentum. Our aging populations make this a pressing need. Contrary to the image (by now belied) of spiraling population numbers, by 2040 more than 20 percent of the population in many countries will be over 60 (the ratio in the United States today is lower). The need to support the ranks of the elderly will create serious problems for government-run pension systems, with the attendant fiscal pressures.

We should capitalize on the current international environment of better prices for commodity exports and relatively low interest rates, to turn growth around. Such favorable conditions come after many years of severely weakening terms of trade. They will not last forever, so it behooves us to swiftly return to a strong growth path.

The IDB Group and the Private Sector

I would like to spend a few moments on the private sector's importance for this effort. The private sector accounts for over 80 percent of investment in our countries, making it the engine of growth and job creation.

The past 10 years of Multilateral Investment Fund support for projects in the private sector, especially with microenterprises and small businesses, have been very constructive. We hope the donor countries will continue to support this initiative by allocating new resources to use for innovative projects that generate growth and employment. We also urge Bank member countries that are not yet MIF members to join in this replenishment exercise.

During this past year, I had the honor of chairing an External Review Group tasked by the Bank's Board of Executive Directors to study how the IDB Group can play a more significant role in supporting the private sector. We reached the conclusion that there are two priority areas: support for small and medium-sized enterprises, which have limited access to credit and often operate outside the mainstream economy; and support for private infrastructure, especially roads, ports, and water and sanitation systems. The IDB's current structure for delivering assistance in these two areas is limited: the Corporation is too small, the Private Sector Department is too isolated from the Corporation, and there is little linkage between these two and the area of the Bank that is promoting such necessary reforms as a structure for local lending to the small and medium-sized enterprises that make up most of the private sector, so as to enhance productivity and create more jobs. The External Review Group studied a number of possible models and, after extensive discussion within the group and with the Boards of the Bank and of the Corporation, recommended that the IDB Group merge its activities into an expanded, restructured Corporation that would focus principally on the two areas I have described here.

Transferring to a restructured Corporation the resources currently allocated to the Private Sector Department would raise the Corporation's profile in the region without the governments having to make new infusions of fresh capital. The new Corporation could therefore address real priorities: supporting small businesses and remedying the region's considerable infrastructure shortfalls. We believe that the time has come to look seriously at this proposal, which is the culmination of a series of studies and task forces reaching back a decade.

Final Remarks

I would like to make two more observations. The first concerns the importance of welcoming leading Asian countries into the IDB family during the coming year. We need to broaden the IDB network to countries that are managing their economies with great success and which represent the most dynamic region for international trade. Only good things can come from increased institutional exchange with these countries, which account for a growing share of our region's international trade.

One final point, before I close. As we all know, the industrialized countries are discussing who will be the next Managing Director of the International Monetary Fund. While this question is not directly related to this meeting, I believe that Latin America should have a say in that process. We are minority voters in the IMF. Unfortunately, however, the region's countries have been the largest IMF borrowers in recent years. We know that there are excellent European candidates, and no doubt they will all have our support. Yet I believe—and I hope the other Governors for Latin America and the Caribbean concur—that the selection process should take into account the successful candidate's familiarity with emerging-market countries, especially those of Latin America.

The world has changed. Bretton Woods was 60 years ago. The region's views need to be considered in those faraway capitals where such a far-reaching decision will soon be made.

I would like to express my deep appreciation to President Iglesias for his invitation to address the Annual Meeting of the Boards of Governors in my capacity as Executive Secretary of ECLAC. I would also like to express my warm thanks to the Government of Peru for its hospitality.

As has been noted during these past few days, the prospects for 2004 are favorable. ECLAC's most recent estimates indicate that the region may grow at close to 4 percent. This projection is primarily associated with a more favorable global economic environment. We interpret these results from a dual vantage point. On the one hand, the data point to a reversal of the trends witnessed in the past few years. On the other, however, the region has yet to recover from the effects of the crisis that occurred more than six years ago. The slow pace of this process has created new difficulties that have compounded the long-standing weaknesses of Latin America and the Caribbean. Hence the need, at this juncture, to take full advantage of the potential offered by this more favorable economic context, while bearing in mind the constraints and opportunities that it may entail.

First of all, there are clearly risks on the horizon. The largest economy in the world has been building up fiscal and external imbalances that will surely drive up interest rates. The question is simply when and how swiftly the adjustment will take place. Although we do not foresee problems in 2004, this is a warning signal that should be heeded.

Second, all the projections indicate that the prices for a number of the products exported by our countries will improve. As suggested by a number of current experiences, and given the marked instability of those prices, the fiscal revenues derived from these resources should be used as a tool for smoothing out the business cycle more effectively than we have in the past.

The region also needs to consolidate other trade channels, in addition to its traditional commodity exports. The development of an export base with higher value added that draws upon existing comparative advantages and that is capable of incorporating new technologies and providing a stronger stimulus for job creation is a task that still lies ahead. In addition to market access, we need to mount a major productive development effort in order to take advantage of these opportunities.

Third, although the countries have worked hard to overcome inflationary pressures and to put public finances on a more solid footing, they have not been able to use fiscal and monetary policy tools to produce the countercyclical effects they had hoped for. Within the context of the positive outlook for 2004, the conclusion is clear: economic policy must capitalize upon the growth phase of the cycle in order to overcome the major constraints that have traditionally limited the effectiveness of fiscal and monetary instruments.

On the social front, however, the panorama is far from encouraging. Poverty and indigence in the region have increased: 227 million people (44 percent of the population) are now below the poverty line, while 20 percent are living in extreme poverty. Open unemployment is verging on 11 percent. This situation demonstrates the serious difficulties that the countries of the region are having in reaching the shared development goals set forth in the Millennium Declaration. To illustrate this point, we might take a moment to analyze where the region stands in terms of the achievement of the Millennium Goal relating to poverty. ECLAC data indicate that, unless improvements are made in income distribution, in order for the extreme poverty levels of 1990 to be halved by 2015, we would need an average growth rate of around 3.6 percent over the next 12 years; achieving the more ambitious goal of halving the total poverty rate would require a growth rate of close to 5 percent per year. These figures have to be compared to an annual growth rate over the past 13 years of just 2.6 percent. What is more, this average conceals differing situations. Whereas, at one extreme, Chile and Panama appear to have already reached the goal, the countries where extreme poverty rates are above 30 percent would have to grow by around 7 percent per year in order to do so. I would like to emphasize the fact that, in a region that exhibits the highest levels of inequity in the world—indeed, in various countries, the average income of the richest 10 percent of the population is 20 times higher than that of the poorest 40 percent—assuming that income distribution will remain constant would appear to be morally inadmissible. According to our estimates, small improvements in income distribution would considerably reduce the growth rates needed to achieve poverty reduction goals.

In the area of education, the broad coverage of the primary education system in the region (90 percent) makes it feasible to reach this goal before 2015. It would therefore be desirable for the middle-income countries to set themselves a more ambitious goal: the achievement of universal coverage for secondary education. Meanwhile, although unemployment and poverty have a greater effect on women, all the indicators show that women are achieving higher skill levels than men. It thus appears that one of the elements that has been associated with gender inequity in the region for decades may now be changing.

Next year, when we will be 10 years away from the date set for fulfillment of the Millennium Development Goals, ECLAC and other United Nations bodies, together with the IDB, will evaluate the extent to which the region has fulfilled its commitments under the Millennium Declaration. We want to make it clear, in no uncertain terms, that in order for the countries of the region to succeed in achieving the Millennium Development Goals, the developed countries must fulfill the commitments to provide assistance and financing for development that they have made in relation to the eighth Goal and, subsequently, in the Monterrey Consensus. As things stand now, this goal is far from being achieved.

Our chances of reducing these levels of social exclusion are closely linked to our economies' performance in the short and medium terms, since the profile and dynamism of job creation are key variables in generating income for the poorer sectors of the population. Yet, in addition, we all know that the economy alone cannot solve the problem. Public social expenditure performs an essential function. The region has raised its levels of social spending, but it clearly needs to make more headway in this direction. Above and beyond improvements in the efficiency of expenditure, gradual increases in the level of public sector revenues are needed in various countries. If decisive steps are taken in this direction, then the better news that 2004 appears to be bringing us may improve our chances of achieving the Millennium Development Goals and thus afford some relief from the hardships that nearly half the population of our countries endures each day.

In view of the substantial challenges confronting Latin America, and given the need to consolidate a form of economic and social progress that is in line with our nations' aspirations and expectations, ECLAC stands ready to take an active part in this undertaking. There are two dimensions of this situation to which I would like to draw your attention.

The first is the challenge of increasing our region's productive potential within the framework of a globalized economy, an economy that is now more open than in the past but that is also subject to a high degree of financial volatility and unequal access to product markets of vital interest to Latin America and the Caribbean.

The debate of recent years has emphasized the importance of maintaining macroeconomic balances and adopting efficiency-enhancing reforms, and the countries of the region should pursue these tasks on a continuing basis. It is true that a great deal has been accomplished, but the results are clearly unsatisfactory. Economic growth is not occurring spontaneously even though the countries now have a healthier macroeconomy, are more open to trade and have, in many cases, carried out sensible institutional reforms. Nevertheless, the macroeconomic environment has been marked by sharp fluctuations in demand and instability in interest and exchange rates. What is more, productivity gains are contingent upon a capacity for the accumulation of knowledge and innovation, that is, the adoption, adaptation and creation of technology. This, in turn, calls for active policies and strategic networking by the public and private sectors. There are no simple, generic formulas for the establishment of such links. At the forthcoming ECLAC session, to be held at the end of June, we will be deliberating with the governments on these issues.

The second dimension is the need to complement and support this productive development effort through regional integration. Early on, ECLAC pointed out the potential offered by integration as a form of open regionalism. Now, there is reasonable room for doubt as to what the future will bring. The proliferation of bilateral trade agreements between Latin American and Caribbean countries and the United States is making it more difficult to form the necessary strategic partnerships within the region. Furthermore, many of these bilateral agreements have the effect of curbing intraregional trade and raise questions as to the form that the hemispheric integration agreement will ultimately take and as to its possible contribution to the formation of closer linkages for the economies of the region.

In short, the essential items on the immediate agenda for ECLAC are to gain a better understanding of the current situation and to draw lessons that can be used in strengthening the productive development of Latin America and the Caribbean and ensuring its sustainability as the region's economies continue to become more open and more integrated. Of course, our interest does not stop here. The linkages connecting labor markets, capital markets and international migration are closely associated with the above factors. We understand that these issues, together with the more efficient social policy that is essential in order to achieve the Millennium Development Goals, are vital elements in dealing with our countries' burdensome legacy of poverty and distributional inequity.

ADDRESS BY MR. ENRIQUE V. IGLESIAS, PRESIDENT OF THE INTER-AMERICAN DEVELOPMENT BANK AND CHAIRMAN OF THE BOARD OF EXECUTIVE DIRECTORS OF THE INTER-AMERICAN INVESTMENT CORPORATION

Let me begin by conveying my sincere gratitude to the Government of Peru for its kind invitation to stage this Forty-fifth Annual Meeting of the Board of Governors of the Inter-American Development Bank and Nineteenth Annual Meeting of the Board of Governors of the Inter-American Investment Corporation in Lima.

We return to Lima 33 years since we last held an Annual Meeting in Peru, a country with which the Bank has been closely associated since its very beginning. Its first loan was to Peru, in 1961, for a water and sanitation project in Arequipa, the country's second largest city. That first operation in a way defined the institution's vocation for social development and its commitment to expanding the frontiers of development banking. It seems fitting today to invoke the memory of Felipe Herrera, that bold visionary who, as the Bank's first president, set our institution on its course to help combat poverty and enhance social equity across the region.

As one of the founding members of the Bank, Peru has been an active participant in the life of our institution for decades and an inspiration to all of us as it has risen to challenges, essayed solutions, and shared its ideals. As the eminent Peruvian historian Jorge Basadre once reminded us, "just as the fundamental law of economics is not accumulation but rather the use of material goods to satisfy the needs of humankind, the fundamental law of culture is not to amass knowledge but rather to adapt knowledge to human beings so they can fully realize their destiny."

The Bank's core mission is to work with and alongside its borrowing member countries to help all the region's people fulfill their destiny. Sadly, large segments of our population have become disillusioned at the slow pace of progress in improving their social and economic conditions and are even questioning whether we have chosen the right path towards greater social justice. Let me offer some thoughts on where we are and how we may move forward.

I. REKINDLING ECONOMIC GROWTH

After five years of sluggish economies and worsening social conditions in most Latin American and Caribbean countries, the region stands poised to enter a new and, hopefully, sustainable chapter in its growth, with prospects for improved quality of life for its people.

Since we gathered a year ago in Milan, the clouds of political and economic uncertainty have lifted and the region's growth prospects are distinctly more promising, by virtue of a combination of favorable external and domestic factors.

On the external front, the expansion of the advanced economies along with robust growth of China's economy have helped boost trade flows and raised the prices of commodities that comprise most of the region's exports. Meanwhile, U.S. interest rates are at a 45-year low, a positive factor in a region as indebted as Latin America. Funding flows and foreign direct investment which had plummeted in recent years are picking up.

The steep devaluation of the dollar, in which the region transacts so much of its business, has made Latin America and the Caribbean far more competitive in non-dollar markets. All of these developments are pushing up growth rates across the region, albeit with some differences depending on countries' individual circumstances.

Just as important have been country decisions to hold fast to fiscal discipline during the downswing of the cycle, at no small sacrifice, and to opt for prudent management of monetary policy. The steep devaluations that followed in some countries are also making the region's economies more competitive in the global marketplace.

In light of these gains, forecasters are predicting roughly 4 percent economic growth for the region in 2004, a vast improvement over the previous five-year average that barely reached 1.3 percent.

Welcome as this turnaround may be, we cannot be complacent. Externally driven improvements in an economy are rarely long-lived, as the region's history, and world history generally, can attest. Sooner or later we can expect to see adjustments in the industrialized economies, particularly the United States, which could affect the global business cycle, interest rates, and commodity prices and trigger currency realignments. The ensuing impact on the region's economies will be determined by the nature and timing of the adjustments and, above all, on the degree of policy coordination among the advanced economies.

How, then, should we handle the current upswing in the region's business cycle?

Very carefully, when projecting into the long term, and building on the favorable situation in the years immediately ahead in order to solidify economic reforms that have worked well, revisit and reconfigure any that have fallen short, and gear up for reforms still needed in order to enhance economic efficiency and thereby deliver greater social benefits to the collective.

With all this in mind, I would like to draw your attention to three issues that are relevant across the board, even with due regard to the particularities of individual countries.

First, managing the economic recovery so as to make economies more resilient to shifts in the business cycle.

Second, increasing the social dividends of economic growth to reverse the social deterioration of recent years, and heightening the social returns to economic policies.

Third, bolstering countries' negotiating capacity both individually and collectively in preparation for major international negotiations on the horizon.

Managing the Economic Recovery

I would like to outline four policy areas that are of particular importance at this juncture.

Strengthening Public Finances

Public finances have come under considerable stress over the last five years. Public revenues as a share of GDP have held more or less steady in a range of 24 to 26 percent but governments have had great difficulty trimming current expenditure, on account of interest on the debt plus other inflexible public expenditures. The current account fiscal deficits in the region's seven largest economies rose from less than 2 percent of GDP in 1997 to close to 5 percent by 2002. The brunt of the adjustment was borne by public investment expenditure, which in 2002 was lower than interest payments on the public debt.

Given the already deficient state of economic and social infrastructure in the region, this situation is not sustainable. The breathing space that may be provided by a period of moderate growth must be used to improve tax administration, modernize the structure of taxes and make public expenditure more efficient. There is no doubt that credible public finances are important for stability in the short run and essential to underpin growth in the medium term and beyond.

Governments throughout our region are looking for ways of reversing the decline in public investment, given the adverse implications of this trend for long-term growth prospects and the countries' ability to achieve their development objectives. In a bid to augment investment some countries are laying the groundwork for public-private partnerships, as a means of tapping private sector financial and other resources to improve the scale, quality, and sustainability of infrastructure investment for the provision of public services. The IDB is contributing to this encouraging development through a number of initiatives, among them a study with the International Monetary Fund and the World Bank on a new methodology for treating investment expenditure in formulating macroeconomic program goals.

Reducing Public Debt and Enhancing the Debt Profile

Latin America and the Caribbean today are struggling under a very heavy debt load. Much of this burden reflects the weight of external borrowings and the effect of exchange rate fluctuations. Devaluations of the real exchange rate in recent years contributed to a rapid rise in the average debt-to-GDP ratio for the region from 37 percent in 1997 to 51 percent in 2002.

Debt service has become such a heavy charge on government revenues that many countries are now giving priority to public debt management to shield themselves against the risks that the dynamism of global financial markets can create. Latin American and Caribbean countries are especially vulnerable to volatility in interest rates, exchange rates, and commodity prices, and their financial authorities are continually seeking ways of spreading the risks to which public budgets and the economy overall are exposed.

Despite the U.S. Federal Reserve System's declared patience, interest rates are likely to climb with that country's economic recovery. Experience shows that a 200 basis points rise in U.S. interest rates translates into a 500 basis points increase in the cost of external financing for Latin America and the Caribbean. In today's circumstances, governments could face significant fiscal adjustment to meet the increased cost of debt servicing, the effects of which could choke economic growth. A clear priority is to seize the opportunities created by the current low interest rate environment to try to extend debt maturity profiles and bring the debt-to-GDP ratio to a sustainable level. Prudent external debt management that capitalizes on these opportunities is the countries' best and straightest course.

Bolstering Financial Systems

Financial intermediation appears to be stalled in many countries. In the region's seven largest economies, banking system credit to the private sector has fallen by 20 percent in real terms since 1998, even though banks are liquid and interest rates stable. The problem is not one of constraints on the supply side; we seem to be caught in the grip of weak demand from the real economy and risk aversion on the part of lenders.

Demand could be expected to pick up as businesses see new opportunities in a growing economy and a possible reactivation of investments. Regulators have to be on their guard, therefore, to prevent the recurrence of the kind of euphoria that in past upswings resulted in the accumulation of bad debt and currency mismatches. In the past that unwelcome mixture has sparked banking crises that carried a high fiscal cost, and was one factor behind the buildup of debt.

The region has done a great deal to strengthen and enforce prudential regulations for financial activity but, in many countries, regulatory systems are still too weak and there is insufficient legal protection for creditors. Countries need to finish creating a suitable regulatory and oversight framework for vibrant financial institutions in order to reduce the risks to fiscal and overall economic health in the years ahead.

Fostering a Friendly Business Climate

Sustained economic growth at a healthy rate will require a much higher level of investment than we have managed in Latin America and the Caribbean in recent years. Investment is at its lowest level in a decade, some 20 percent below the 1997 peak. Macroeconomic stability will provide the needed framework for sustained growth, but that will not be enough. A host of institutional and related reforms are necessary to regain the confidence of investors. Too often in recent years has one country or another changed the ground rules unilaterally, triggering uncertainty among investors about what might happen elsewhere in the region.

What is needed today, in contrast to the sweeping reforms of the early 1990s, is a more selective effort to gain credibility and thus build firmly on everything the countries have accomplished to date. In order to train the spotlight on this goal, late last year the Bank invited officials, private investors and academics from most of our member countries to participate in a Public-Private Summit to exchange ideas on the business climate and the way forward. The Bank used that very visible opportunity to launch its 'business climate initiative' that is an open invitation to each country to work with the Bank to remove specific impediments to higher investment in its economy.

Improving the Social Dividends of Growth

When our economies grow slowly or not at all, there is a high social cost borne disproportionately by the poor. The political cost in lost momentum for reform is also high. Since 1998 a majority of Latin American and Caribbean society has been losing confidence in the possibility of improvements in quality of life in an open, market-friendly economy. This is not surprising in face of the growing inequality of the distribution of income, deteriorating social infrastructure, rising unemployment, and the reversal of a decade-long trend of reductions in the share of the population living in poverty. In 2003 there were 20 million more poor people in our region than in 1997.

Accordingly, at this threshold to a period of renewed growth our countries have to pay as much attention to the distribution of the social dividend as to building macroeconomic stability and a propitious investment climate, by adopting public policies that help create jobs and opportunities for the poor.

Let me mention here some policy priorities to that end.

The Labor Market

Affording remunerative employment to the largest number of people of working age is the principal means for individuals to move into the mainstream of society and for the fruits of economic progress to be shared. Our economies have been underperforming and, in fact, the stubbornly high unemployment is one of the major sources of discontent with economic reforms in Latin America and the Caribbean. Last year, open unemployment in the region averaged a record 10.7 percent; in several countries the unemployment rate topped 15 percent.

Although labor legislation in general seeks to protect workers from the insecurity caused by swings in the economy, it can have the perverse effect of discouraging permanent employment in the formal economy, and is especially a barrier to young people and women. One imperative is to remove these disincentives and build effective information, training and surveillance systems to encourage flexibility in labor markets.

Social Expenditure

It may surprise many of you to hear that in Latin America and the Caribbean during the last decade governments increased social expenditure, in real terms, by about 58 percent per capita. However, the results have been disappointing. Throughout much of the 1990s a sizable share of this increase was funneled to restructuring social security systems. Had those structural reforms been postponed the burden on the public finances could only have been more onerous. We must recognize, however, that social security benefits formal sector workers, to the exclusion of the majority of the poor who toil in the informal economy.

One encouraging development in recent years is the concerted effort made in many countries to protect public spending for education and health, even in times of tight budgets. However, it is imperative to get better value for money as we move forward. Let me underscore three dimensions to improving the quality of social spending outcomes:

- Higher efficiency of expenditure;
- Focus on greater social inclusion; and
- Encouraging greater participation by citizens.

Efficiency of Expenditure

All of our countries subscribed to the Millennium Development Goals (MDGs) at the United Nations Millennium Summit in September 2000 and reiterated their commitment at the Summit of the Americas in Quebec City the following year. Many measurable targets were set, for example for reducing poverty, lowering infant and maternal mortality and containing HIV/AIDS. These targets are at once a stiff challenge and a yardstick against which to measure progress toward greater efficiency in social expenditure.

In this era of fiscal restraint, it is incumbent on each country to make sure that every outlay has a clear purpose and to check its progress systematically. Of course, each country should challenge itself to do even better than the MDGs—for example, most of us should be aiming to achieve higher coverage and quality in secondary and tertiary education since we long ago achieved universal primary education. One milestone on this path was last November's Declaration of Brasilia, in which a number of heads of state, ministers, and civil society representatives pledged to push for attainment of the MDGs. This is a significant step forward on the way toward 2015 which is the target year for achieving the Millennium Goals.

Enhanced efficiency of social expenditure must go hand in hand with efforts to achieve greater progressivity, targeting society's most disadvantaged. Today, as we again look to a period of growth, we have to seize the opportunity to build robust social protection systems that will work in good times and, more importantly, when times are bad.

There are flagship social protection programs in some of our countries that hopefully will inspire others to develop similar operations tailored to their own circumstances. The common purpose is to protect benefits for society's poorest and lay the groundwork for breaking the links that are bequeathing poverty from one generation of a family to the next.

Social Inclusion

Inequality in income distribution in Latin America and the Caribbean is part and parcel of social exclusion, particularly exclusion on the basis of ethnicity and race. Indigenous and Afro-Latin populations are, as a group, the least educated, the most afflicted by disease and malnutrition, the poorest of the poor. Targeting spending is a proven way of addressing social exclusion, but much more important is the political leadership to spark changes in attitudes, enact legislation and put it into practice, and develop intelligent positive discrimination schemes to give voice to these and other historically excluded segments of the population such as persons with disabilities. These are the building blocks of social change which is, in turn, the foundation for lasting improve-ments in quality of life as sought with the Millennium Development Goals.

Citizen Participation

The social dividend accruing from higher economic growth will also be greatly enhanced to the extent that citizens partner with government to help decide on and chart the course ahead. The ethos of the welfare State should steadily give way to more active participation of the citizenry in decision-making. We must use the resources of society at large to make inroads against poverty and social exclusion. Corporate citizens could play an especially important role here, not merely out of a sense of charity or philanthropy but because it is good business.

International Trade Negotiations

Let me turn to a topical issue of transcendental importance for opportunities for economic growth, job creation, social progress, and improved political relationships in the years immediately ahead: the regional, hemispheric, and global trade negotiations that are currently engaging the attention of all our countries.

Trade liberalization is one of the cornerstones of the structural changes at work in Latin American and Caribbean economies. At first, in the late 1980s and early 1990s, many countries unilaterally lowered tariff and other barriers to trade. Today the effort is dominated by negotiations in regional, hemispheric, and global forums, including landmark arrangements between countries at distinctly different levels of development. These simultaneous negotiations severely test the capacity of many countries, especially the smaller nations, to protect and advance their interests.

The global Doha Development Round and the Free Trade Area of the Americas (FTAA) initiative have been at center stage over the last year. Both processes have lost some momentum over differences of opinion on such issues as trade in agricultural goods and other topics. Since most developing countries—a number of them in our region—have a comparative advantage in agricultural production, rationalizing agricultural trade is a unique opportunity for them to reap the economic benefits of trade liberalization. This issue may well finally have to be resolved at the global level in World Trade Organization negotiation forums.

What I would like to stress here is that even with the impasse in agricultural trade talks there is room for progress and gains in the FTAA process. The key is to have a clear, common agenda and work step by step toward the ultimate objective, with due regard always to the particular interests of the different parties to the arrangement. Negotiations are continuing between subregional groups and the United States, including the Central American Free Trade Agreement (CAFTA).

Bilateral arrangements between the United States and subregional groupings in Latin America and the Caribbean are not, however, a substitute for a full FTAA. The FTAA is a process rather than an event. As such, it is a regional public good that opens opportunities for cooperation in areas beyond immediate trade liberalization. For example, the atmosphere of cooperation created by trade negotiations has unleashed a major physical-integration effort for investment in regional infrastructure in South America (the IIRSA) and from Mexico to Panama (the Puebla-Panama Plan). As countries engage one another, deeper forms of cooperation and benefits will emerge that will anchor the region's structural reform and enhance the quality of its institutions.

The Bank has been closely involved, along with the Organization of American States and the United Nations Economic Commission for Latin America and the Caribbean, in the secretariat function of the FTAA negotiations. Equally important, the Bank has been assisting countries in building capacity to undertake hemispheric and global negotiations and offering technical support to help with the difficult task of implementing the corresponding changes in domestic legislation and institutions.

More important yet is the critical support the Bank has been providing to some countries to enhance their ability to compete for business, including planning for an expanded, high-quality integration infrastructure.

What needs to be stressed here is that the true challenge of this process is to translate development promise into real investment, exports, economic growth, jobs, and poverty reduction—in short, into quality-of-life improvements. The negotiation phase, difficult as it may seem, is only the beginning. As you know, the Bank has developed a set of initiatives such as the competitiveness program, funding for integration infrastructure, and loans to support fiscal and customs system reforms, to help countries through the painful transition and equip them to compete in a global economy without the benefit of preferential arrangements.

The Bank's Charter mandates our institution to work for the development of the borrowing member countries collectively. At the present juncture, this calls for scaled-up efforts to deploy regional public goods to further the cause of integration. Our vocation to promoting integration is perhaps the most vivid proof that we are "more than a bank." It therefore is very gratifying to report that the Board of Executive Directors recently approved special arrangements for funding a work program of regional public goods.

II. STRENGTHENING THE BANK AND THE CORPORATION

Over the past year, we took action to further strengthen our institution and increase its capacity to work closely with the borrowing member countries in their quest for greater social justice. Let me enumerate a few highlights:

- A new Capital Adequacy Policy and associated procedure for fixing a standard lending rate are now in place. This enables the Bank to align its risk management methods and procedures more closely with current international banking practice. You, the shareholders, have every reason to be proud that, thanks to your unswerving commitment to the Bank's financial soundness, our institution can now offer its borrowers stable loan charges that are lower than those of its comparator multilateral development banks;

- Following receipt of the final report of the External Review Group that had been appointed by the Board of the IIC, with the goal of spurring private sector economic activity, the IDB's and IIC's Management and Boards of Executive Directors directed much attention to articulating a vision for the institutions' work in that sphere. While there still are many questions about the benefits of a merger between the IIC and the Bank's private sector window, the Corporation adopted a short-term action plan and is already seeing improvements in process efficiency and financial performance. In the Declaration of Nuevo León adopted earlier this year, heads of state called on the Bank to triple its lending to small and medium-sized businesses and microenterprises. We readily accept this challenge and expect the Corporation to play a pivotal role, along with the MIF, in ensuring that we succeed in the very important work of raising productivity and competitiveness in this sector that is central in the fight against poverty;

- As a follow-on to my commitment in Milan last year regarding the imperative of aligning internal corporate governance of the Bank with the tighter legislation that several of our member countries had recently enacted, including the Sarbanes-Oxley Act in the United States, Management recently forwarded to the Board of Executive Directors a set of broad recommendations covering such areas as corporate governance structure—principally the creation of a separate Audit Committee; relationship with external auditors and their responsibilities; and enhanced disclosure in financial reporting. In the course of the past year, we adopted a staff rule to protect whistleblowers, established a fully independent Office of Institutional Integrity, adopted a Code of Ethics for members of the IDB and IIC Boards of Executive Directors and the MIF Donors Committee, and made substantial progress in amending the Code that applies to staff;

- The procurement of goods and services is a central activity in our line of business and also a potential space for corrupt behavior. Last year we hired consultants to assess our procurement rules and practices, both for our projects and for Bank procurement. We recently received the final report on Bank procurement and expect to receive shortly the report on procurement in Bank-funded operations. Both reports will make recommendations aimed at ensuring that we work by 'best practices.' This subject is on the work agenda of Management and the Board for the months ahead;

- Another of our commitments in Milan was to launch a process of civil society consultation to frame a new Information Disclosure Policy. I am pleased to inform the Governors that the policy was approved last November. Progress is also being made on a proposal to renew the Independent Investigation Mechanism to align it to best practices in our comparators.

III. THE REGIONAL POLITICAL SCENE: THE LEADERSHIP CHALLENGE

It is vital that we continue strengthening and renewing the Bank so it can continue to be an active, reliable partner of its borrowing member countries as they strive to consolidate growth and distribute its social dividends.

In my address to the Inaugural Session of the 1999 Annual Meeting in Paris, I underlined the importance of bolstering our democracies in order to harmonize economic achievements with social dividends. Although I touched on this theme in subsequent Annual Meetings, I feel compelled to return to it once again because it is so critical if we are to be successful in advancing our economies and societies.

Political developments in the region are giving a mixture of encouraging and worrisome signs. That democracy is becoming firmly rooted in the region's major countries is a promising sign, as is the democratic renewal of governments in countries that barely a decade ago were caught up in wrenching political-military strife. Yet another positive sign is that some countries in the region, which are trying to manage severe socioeconomic tensions and heed increasingly insistent calls for change, have been able to absorb and democratically process these tensions and demands, amidst a widespread perception that the public has little tolerance for non-democratic solutions. These are encouraging signs indeed.

On the other hand, political difficulties in some countries in the region today or in the recent past are cause for concern. The media and the citizenry in those parts of the region would appear to have an image of political instability etched in their minds.

Though all the empirical evidence suggests that the people of Latin America and the Caribbean back the liberal democratic system as an invaluable asset, it also shows many of them to be thoroughly disenchanted with how democracy is working and with governments' inability to improve the day-to-day lives of citizens and give them hope for a better tomorrow.

In some cases, discontent reached the extreme of cutting short a presidential term, and there has been more than one episode of civic upheaval. But every case shows that the previous complementarity between political and economic liberalization agendas is suffering the effects of the malaise of over five years of economic recession. Whereas the fruits of more stable economies and reined-in inflation were shared across a broad spectrum of the population, reform and liberalization policies did not always achieve their objective of distributing equitably their costs and benefits. When public policies are captured by private interests, small groups or coalitions typically carry off the lion's share of the benefits, leaving the masses to shoulder the costs.

Disillusioned though some in Latin America and the Caribbean may be with how the democratic system is performing, the majority still backs that system. What, then, are the roots of this worrisome political instability that plagues some countries in our region? One factor, certainly, is how gaping social disparities or unethical behavior in the high echelons of government and the corporate world are eroding the credibility of institutions and the political leadership, but this does not appear to be the whole explanation.

Expert analysts of the region's political scene are warning us of the need for the political leadership to pay attention to the political system and its workings. In some countries the instability is fueled by the fragmentation of political parties, which are facing the challenge of changing or disappearing. The expert consensus is that democracy needs solid, institutionalized political parties driven by a long-range vision, ideas, and agendas. The agenda to renew the party system, now being pursued, and to reconfigure the electoral system, calls for serious reflection on the part of political leaders.

Overall, it would appear that the electoral and political system is not, in all cases, appropriately aligned with the requirements of a modern, participatory democracy that makes it possible to build consensus and forge agreements on policy priorities and on institutional, political, and economic reforms that have such a significant impact on the workings of society in the long run.

As the issues of institutions and politics have moved onto the development agenda, the Bank has been working with the Organization of American States, the United Nations Development Programme, and other agencies on research and outlining suggestions to improve the working of our democratic political system. The fruits of this work have been shared with the member countries in the form of publications, seminars, and conferences.

In light of the many ways in which public policies can be captured by private interests, it is essential for the Bank to assess ex ante who stands to benefit from the reforms that it is supporting and build in mechanisms to ensure a broader distribution of the anticipated benefits. This means identifying and mitigating those risks that could keep public policies from addressing general societal interests and ensuring that the fruits of progress are equitably shared.

I believe that this is a fitting note on which to conclude my remarks to you today. If our countries are to seize the opportunities now opening up, it is vital that they move quickly to surmount the most serious instability problems and dispel political uncertainty. Though growth will come from hard work and sustained savings, investments, and technical change in the broadest sense, it also will depend on the international climate and the depth of our region's integration, by way of trade and investment, into an increasingly interdependent, competitive world. In the long run, the region's advancement will depend on the ability of its leaders to build sturdy, rule-of-law institutions which endow the economy with resilience to shocks and fairly distribute the benefits and costs of growth. That is the best and only course for enduring peace, stability, and progress in our region.

I bring you warmest greetings from a sister country that has thrown open its doors to welcome you with conviction and with hope for the future.

On behalf of Peru, I am grateful with all my heart to the Governors of the Inter-American Development Bank and in particular to its President, Enrique Iglesias, for their decision to hold the Forty-fifth Annual Meeting of the Board of Governors of the IDB here in Lima. This gesture is for us a demonstration of confidence, and we are honored by it.

The IDB, and you, Mr. Iglesias, are key players in meeting the daunting challenges of a changing Latin America.

I know that several countries of Asia are seeking to join the IDB. Peru welcomes their interest to draw closer to our region, and sees this as recognition of a people that, with great effort and in the midst of many upheavals, has set out resolutely on the road to economic growth with a human face, growth that will make democracy not only a political ideal but also a social reality.

The IDB is a friend and an ally in Peru's development. As I pointed out last night, the first loan that the Bank made was to Peru, in 1961, for a drinking water project in Arequipa. The Bank's continuing commitment has been such that over a period of more than 40 years, it has provided loans exceeding US$6 billion, primarily in support of productive and social development projects.

Today in this hall we have assembled decision-makers in both the public and private spheres, finance and development experts from throughout the Hemisphere, and distinguished guests from 46 countries around the world.

The Latin American agenda today is marked by great issues that are closely linked with the Millennium Goals established by the United Nations. They pose challenges for reducing the high rates of childhood malnutrition, the high levels of infant mortality, the disease of tuberculosis that still threatens us, and HIV and AIDS. We have committed ourselves before the United Nations to address these challenges. And there are other challenges too. How can we generate more public investment to build highways to link our countries together? How can we make greater and better investments in education, in schools and hospitals, in electricity grids, in drinking water? How can we meet the high expectations of society that have been building up in Peru and in the region for many years? How can we avoid placing democratic governance at risk in the region, threatened as it is by pressure from the streets, and at the same time manage the economy responsibly? How can we ensure that democracy will listen to Latin Americans' calls for more jobs, higher incomes, less poverty, and greater dignity?

Our countries have made great efforts to be responsible members of the international financial community, and we will continue with those efforts. Yet the reality is more complex, as Enrique Iglesias has mentioned. Democracies in transition, such as Peru, are floundering in the wake of rising social demands.

Today more than ever, Latin America needs more financial breathing room so that it can increase public investment, together with the private investment that, in the final analysis, is the engine of economic growth. I say this on behalf of a country that can point modestly to some real macroeconomic achievements: we have grown on average at 4 percent annually in the last three years, after emerging from four consecutive years of recession. We have one of the lowest inflation rates in the region, a manageable fiscal deficit of 1.9 percent, and international reserves that are at their highest level in 40 years. We have credibility with the international financial system, as reflected in a country risk index that is the lowest in Peru's history, and that is indeed below the Latin American average. Private investment is growing, not as fast as we might like perhaps, but nevertheless at around 6 percent. Our currency, the sol, is one of the most stable in Latin America. I say this with all modesty and caution.

Since the beginning of our term, we have based our policy squarely on two central themes: responsible management of the economy, and a greater role for high-quality social investment that can, over the short term, alleviate some of our people's pent-up expectations.

Yet I must be blunt. Despite these macroeconomic successes, as the poor of our countries will tell us, the benefits of economic growth are not trickling down to them. In other words, our macroeconomic stance may be sound, but people's pockets are empty.

The man in the street sees things quite differently. He has no time for abstractions—he has to cope with day-to-day realities. The banging of pots still fills the air. We know that we are competing for investment capital and that we must not fall into that vicious circle where politics becomes ever noisier while investment, growth and employment decline, to be followed by more poverty and more political noise. That is a pernicious cycle.

There is a high political price to be paid for delays in delivering the benefits of macroeconomic growth. That is the price of governing responsibly. We are a clear example of that fact, and I come before you today to reaffirm my conviction that we must continue on these two tracks, whatever it costs us in popularity, and I do so because I am convinced that populism is not the answer.

The experience of the 1980s provided a clear lesson of what we must not do. The 1980s were a lost decade for Latin America, one that saw the debt problem deepen and that imposed the heavy tax of hyperinflation on many countries.

In Peru, the 1990s were supposed to bring progress in resolving these problems, and yet that decade too was at least half-lost. Peru defeated hyperinflation and it rejoined the world financial community, it put down terrorism, but it did not make any substantial inroads against unemployment and poverty. In fact, poverty in Peru doubled during the 1990s, and the number of Peruvians living in poverty rose from 7 million to 14 million.

Just as our citizens must understand that fiscal and monetary discipline is a prerequisite for attracting the investment that will fuel economic growth, which in turn will generate productive employment and incomes, we must also understand that without social peace our investments will yield us little.

In Peru, we have moved some way towards achieving this synthesis. We have introduced discipline into macroeconomic management, particularly on the fiscal and monetary fronts, and the indicators are there for all to see. We have made great efforts to boost employment and we now have investment commitments for the year 2004 amounting to some US$4.8 billion.

The Camisea gas megaproject enters its second stage this year with an additional investment of US$2 billion for processing liquid gas for export. Thanks to this project, we will bequeath to the next government, to whomever the people elect, some US$600 million in gas exports a year, starting in 2006, when I shall no longer be President.

For this year, we have the start-up of exploration for a mining center in one of the country's poorest departments, Apurimac. That mining center will produce copper and gold and will require an investment of around US$2 billion.

The Antamina project is of a similar magnitude. This year will also see investment of around US$300 million in the Bayovar project to produce sodium sulfate for fertilizers. Mining exploration in the Alto Chicama will also get underway this year, with an investment of around US$350 million, and other exploration projects are planned, amounting to US$180 million.

We are working hard to reach free-trade treaties with the United States, with Europe and with Asia.

We will not enjoy any political benefit from these efforts. We are working for the next government, and for future generations. Yet even with these prospects, I must give you my honest opinion: while optimism is a good thing, it is not enough.

Latin America needs to grow by between 7 and 8 percent over the next 15 years, in order to regain the per capita income it had in 1970. In terms of magnitude, for Peru to grow between 7 and 8 percent with its current productive infrastructure, will require new investment amounting to some US$8 billion. This means that the State has a major role to play in creating a climate of political, economic, social and legal stability, with clear and transparent ground rules.

We know that we are competing worldwide for investment capital, and that capital will go where there is legal stability. That is our responsibility.

We have a great task ahead of us, to find innovative ways to meet the demands of responsible economic management and to reconcile those demands with the cries in the streets. That is our challenge for the next decade, and that is why we are here. That is why the Annual Meeting of the IDB faces today a vast agenda that for some time now has gone beyond the strictly financial sphere.

Above all, we must act with initiative and optimism. The worst thing that could happen to us would be to fall into the trap of infectious pessimism. The phrase "can't do" is not part of my vocabulary. Experiences such as that of Villa El Salvador and the Gamarra textile district—and Peru's other Gamarras—prove that indeed we "can do." Here we have thousands of microentrepreneurs who never went to a famous university yet today are making products that can compete in price and quality on both the domestic and international markets.

There is an enormous potential in our countries that has not been properly integrated into the market and the economy. I am speaking of our poor. The poor of Latin America constitute 44 percent of its population, and yet they are only marginally involved in the productive processes of our economies and the market.

This poverty has to be addressed through public services, schools, roads, bridges, and hospitals. The poor are not waiting for us to give them a fish. They are demanding the chance to learn how to fish, and to do so they need better health care and more schools. We know that this cannot be done exclusively through private investment: we need to increase public investment, and do it more efficiently and with greater citizen participation.

Poverty is not an obstacle. On the contrary, it is paradoxically a window of opportunity for breathing new life into our productive processes and markets. Fifty-four percent of Peruvians are poor people who have no significant role in the productive process, and yet if they did, they would have jobs and incomes. They represent an extraordinary potential market that could buy more of the milk, the bread, the shoes and the stockings that our businesses produce.

It is in the interest of investors to reduce poverty and to turn this untapped potential into a real consumer market.

It is not only our limited execution capacity that stops us from increasing public investment. The problem also lies in the scant maneuvering room we have for increasing public spending and, most certainly, in the constraints imposed by the ceiling on external debt.

Last year, Peru presented a number of proposals to the Latin American Presidential Summit of the Rio Group in Cusco, and they were included in the Cusco Consensus as "innovative financial mechanisms to strengthen democratic governance" in the region.

One alternative, and the most logical one, is to adopt fairer accounting rules similar to those that are applied in developed countries. But changing the public accounts system is a lengthy process. I go back then to our proposal to separate the fiscal deficit into two parts, distinguishing between current expenditure and spending on investment. If we can do this, I believe it would give us greater financial room for increasing public investment.

Several other Latin American presidents and I held conversations with Mr. Koehler when he was Managing Director of the International Monetary Fund. I am pleased to tell you that Mr. Koehler understood the urgency of increasing investment, and he said so publicly a few days before he resigned.

We also know that the staff of the IMF and the representatives of our Latin American governments are working to rationalize the accounting rules in order to approach this issue more realistically. We understand that there will shortly be meetings with representatives of the G8 industrialized countries.

Let me be frank and direct. Speaking for Peru, and I hope for the Latin American viewpoint, I want to see people in the International Monetary Fund who understand our culture and our region. As far as Peru is concerned, I can say unambiguously that we are seeing afresh the candidacy of Mr. Rato of Spain for the job of Managing Director of the IMF. We will be working within the region to this end.

A second and complementary alternative that was proposed at the Rio Summit, and which Enrique Iglesias has already mentioned, is to create regional infrastructure authorities, specifically a South American authority and another for Central America.

Peru is currently investing around US$200 million a year in roads, compared to the US$4 billion required for the IIRSA-Peru network alone. If a South American Infrastructure Authority could increase highway investment by a further US$200 million a year, our gross domestic product would grow by an additional 1.2 percent annually. In fact, if this were to happen in 2004—and I know this is not realistic given the late start—we could grow by 5.7 percent this year, and we could also create perhaps 100,000 new jobs, directly and indirectly.

Let us devote some time and energy to devising innovative mechanisms that will give Latin American countries more financial breathing room so that we can increase public investment alongside private investment, and in this way ensure that economic growth is more sustainable, and that it can absorb the tremendous social pressures that are threatening democratic governance in our region.

To conclude, I have good reasons for being guardedly optimistic about the future of Peru and Latin America. I want to offer my heartfelt congratulations to the Governors of the IDB, to its President, and to the private bank presidents for becoming more understanding without losing sight of the fundamentals.

I said that I came here to reaffirm my commitment not to stray from the course of responsible economic management, whatever that may cost in terms of popularity.

The decisions that my government is making today are not geared to the elections in 2006. When we make decisions of State we are thinking of future generations.

I believe we can be justly proud for having persevered in putting our house in order during the 1990s. There must be no backsliding now, for we face new challenges.

That is the essence of what I wanted to convey to you today. An argument for guarded optimism about the future for Peru and for Latin America. The need to be more creative, to listen to the people in the streets, and to respond more promptly to their just demands, without abandoning our duty to manage the economy responsibly. Greater public investment that will support and reinforce private investment so as to foster more sustainable growth, better governance with innovative management on our part, more participation by civil society, more democracy, and more solidarity.

On this note of optimism about the future of Peru and Latin America, I declare this Annual Meeting of the Board of Governors of the IDB officially open. Thank you all for coming to Peru.

I would like to begin by expressing my deep gratitude to the Peruvian authorities and to Minister Pedro Pablo Kuczynski, our hosts for this Forty-fifth Annual Meeting of the Board of Governors.

This year, our region appears to be emerging from the turbulence of the recent past. We trust that we are witnessing the start of a virtuous cycle of growth. However, we are running behind. The economies of Latin America and the Caribbean have grown by just 1.3 percent a year on average since 1998. This has contributed to unemployment, which affects 16.7 million people in our urban centers. Rural poverty was also exacerbated by the agricultural subsidies of the developed countries. Consequently, we face an enormous challenge.

Forming part of the global economy, maintaining solid foundations and ensuring a stable institutional environment are imperatives. But our recent experiences demonstrate that macroeconomic balance and the free play of market forces are not sufficient to promote the structural changes that are necessary for long-term growth. We have to articulate the problem of investments in infrastructure and recognize the importance of the role of the State in constructing a more prosperous long-term outlook.

Accordingly, President Lula has been advocating, within the international community, a rethinking of the methodology for reckoning the fiscal results of public investments. Today, profitable projects by publicly owned companies with solid track records of good governance are not being carried out on account of fiscal constraints. I believe that we, the Governors of the IDB, should advocate—in collaboration with the International Monetary Fund and the World Bank—a review of the fiscal accounting of economic and social infrastructure projects we finance. IDB and World Bank supervision would provide assurances that such resources are used effectively.

The reduction in public investments is bringing down the demand for external financing. This situation challenges multilateral organizations to develop new ways of contributing to the region's development.

The Board of Executive Directors and Management of the Bank were given a mandate at the Annual Meeting in Milan, first, to create new, flexible and countercyclical instruments for the member countries and, second, to make headway regarding the findings of the External Review Group, with a view to restructuring the activities of the IDB Group from the financial and organizational standpoints, in order to increase support for the private sector in the region.

With regard to the first point, I acknowledge the efforts of Management to identify other forms of financial support, which culminated in the approval of seven new instruments in 2003. However, some of those mechanisms continue to overlook the financial constraints of most of our countries. Like the World Bank, we should also attach greater importance to our institution's role in promoting policy reforms and changes.

The Bank's lending figures for 2002-03 are eloquent. In 2002, one of the worst years in the region's history, when the countries were in greatest need of support, the Bank lent US$4.5 billion less than it could have.

In 2003, lending was also US$2.5 billion below what it could have been; the difference would have been even greater were it not for US$3.2 billion in emergency lending. Investment loans amounted to just US$1.5 billion out of a US$5.1 billion lending program. It is urgent to gear the Bank's lending products to the nature of the demand in the countries.

This is the time for decisiveness. Having approved the new capital adequacy policy, we are now ready to reexamine the ceilings and restrictions on specific instruments. The role of this Board is to provide guidance for the Board of Executive Directors and Management in taking the steps necessary to carry out the Bank's mission.

With the Bank's financial soundness and the effectiveness of its activities secured, I also propose that the Board of Executive Directors be given a mandate to remove specific restrictions on existing lending instruments, allowing the size of loans to vary in function of demand for the different instruments, provided that the sustainable lending level is always respected.

The continued postponement of decisions of this kind is jeopardizing the Bank's historical mission.

I would like to turn now to the matter of the private sector. I share the conviction that the private sector plays and will continue to play a fundamental role in development in the region. Nowadays, a considerable portion of our economic infrastructure is being built and operated by the private sector. A large part of the systemic competitiveness of our economies depends on that sector's performance; and its role in the creation of income and jobs, in economic growth, and in poverty reduction is obvious.

At the Annual Meeting in Fortaleza it was decided, on Brazil's initiative, to establish an External Review Group to study the difficulties faced by the Inter-American Investment Corporation (IIC). We focused our attention on a study of alternatives that would make it feasible to expand the IDB Group's support for private enterprise. In Milan, the Meeting of the Board of Governors underscored the need for the IDB Group to develop and expand its forms of support for the private sector.

One year later, the concrete results of this mandate are still slim. I would like to stress the need to complete—within 60 days, in accordance with the commitment made by Management and the Board of Executive Directors—the work plan for implementing the Private Sector Development Strategy, particularly with regard to expanding the scope of the activities of the Bank's Private Sector Department (PRI).

In that connection, I would like to directly thank the Chairman of the Board of Governors, Mr. Pedro Pablo Kuczynski, for his contribution as coordinator of the External Review Group. The analyses and suggestions in the Kuczynski report are a starting point for guiding the discussions and the decisions we will have to take in the coming months.

I endorse the idea of creating a private sector coordination office, which would cover the activities carried out by PRI, the IIC and the Multilateral Investment Fund (MIF). The coordinator would have the specific objective of implementing actions and formulating a long-range strategy for the work of the IDB Group in this area. This official would report directly to President Iglesias, as head of the entire Bank Group, and would need a strict operating mandate, defined in terms of reference, for a period of one year, which perhaps could be extended for one more. To ensure the coordinator's political neutrality and provide for broad freedom of action, I further propose that the person appointed not be eligible to fill the post of vice president, if one is created.

It is urgent to speed up the interface between the IDB Group and the private sector. We need to work to ensure, apart from the steps already taken by the Group, that we can produce concrete results that will benefit our countries.

I would like to close with a few words on the Bank's role. The IDB has a glorious past. Today it is facing the challenge of adapting to the new reality in our countries, seeking a new focus and new forms of support. It must quickly adjust its instruments to the present needs of its members and, in addition, strive to ensure that those instruments are effective and maintain adequate disbursement levels. I have every confidence that the IDB will be successful in the future as well, in its steady pursuit of these objectives.

I would like to begin by thanking the authorities of Lima for hosting this year's Annual Meeting in this historical and vibrant city.

The projections for higher economic growth this year in Latin America and the Caribbean make us confident that a recovery is on the way. At the same time, the worrisome social and political landscape in some countries suggests a need for vigilance. Social inequality and poverty continued on the rise in 2003, and social unrest and political crisis in a number of countries led to government instability. There is a pressing need to act with resolve in order to ensure that the heightened capacity is utilized to counter these alarming trends. The benefits of growth and economic recovery must flow to all segments of the population. Exclusion is not an acceptable option.

The IDB has taken steps to respond to the challenges facing the region and the differing and shifting needs of its borrowers. Norway welcomes the Bank's new, modern policy on capital adequacy, which is farsighted and aligned with international standards and practices, with an eye to maintaining a sound financial base. The year 2002 saw the adoption of a new lending framework, to be revisited in 2005, and a further set of new lending products was approved recently.

We are not convinced that more flexible and fast-disbursing mechanisms are the answer to the challenges before the region. In fact, the Bank already has a wide array of lending instruments, yet demand for these products is low. In our judgment, the focus should be to improve the investment climate and enhance the development effectiveness of existing instruments, spurring demand for loans that address directly or indirectly the challenges posed by poverty and inequality. To this end, the IDB should work closely with the IMF and the World Bank.

Over the last 12 months, the IDB has adopted various measures designed to sharpen the focus on results in its country programs and operations. A general framework for development effectiveness, however, is not yet in place. It is our hope that the appointment of an official to head this area will speed up the development of a results-based management and culture within the Bank, which should be linked to the Millennium Development Goals. In this context, it will be vitally important to make sure the "results agenda" encompasses the entire Bank through a new system of incentives to align the Bank's functions and human resources to the new system.

A firm country focus is essential for the success of this agenda. It will be no small task to create the sense of ownership that is needed and help develop the borrowing countries' capacity for management by results. Institutional development and the creation of sound and sustainable capacity in the countries calls for a more strategic and coordinated approach over the long term that cannot, as is often the case at present, be confined to isolated projects and short-term advisory assistance. We would like to see the Bank take on a leadership role in promoting dialogue on development effectiveness in the region, working hand in hand with other stakeholders. To accomplish this aim, standard performance indicators, efficient monitoring, and systems to implement results-based management need to be developed in close cooperation with the countries and other donors.

In redirecting the focus to results in the countries, the Bank's programs and strategies will need to be aligned more consistently and broadly with national development strategies (or existing national poverty reduction strategies) through concerted and tight-knit efforts with other donors. The Bank's regional stature gives it a comparative edge by contributing to the sense of ownership at the local level and also in coordinating donor efforts, and this advantage should be tapped further in the future. The Bank has at its disposal the financing instruments that are needed to participate in donor coordination mechanisms, as in the area of sector financing. Greater participation by the Bank in joint initiatives at the country level is an important factor in enhancing development effectiveness and attaining the Millennium Development Goals.

The long-awaited Private Sector Development Strategy for the IDB Group that was recently approved gives us a starting point from which to discuss priorities and various other matters. We welcome this decentralized and integrated approach to private sector development in the countries. In order to build a sound approach at this level, the Bank's strategies for the private sector should be aligned with national development strategies and it should work closely with other stakeholders such as the World Bank Group. In addition, organizing and coordinating efforts within the Bank that are geared to private sector development will be critical to the strategy's success. We would like to reiterate here our interest in seeing the creation of an institutional structure encompassing the IDB Group in its entirety, with responsibility for coordinating the different entities involved in implementing the strategy.

We feel that such a mechanism should be functioning before consideration is given to broadening the private sector development mandate. The contribution of new eligible sectors to the tasks of poverty reduction and pro-poor growth must be the yardstick for Bank efforts to expand its activity with the private sector.

The new Information Disclosure Policy, the review of the Independent Investigation Mechanism now in progress, and the strategy being developed on citizen participation send a clear message to all member countries that the IDB is committed to transparency, accountability, and broader-based participation in its operations. Norway fully supports the IDB in these efforts. In our view, an independent inspection and investi-gation mechanism is vital for the credibility and effectiveness of Bank operations. We are confident that the IDB, like other multilateral development banks, will do whatever is necessary to establish an inspection mechanism that is transparent and independent.

In this same vein, broader citizen participation in the decision-making process is a prerequisite for democratic governance and sustainable development, and we commend the IDB for taking concrete action to broaden community input in the country programming dialogue and implementing operations. Specifically, it is our hope that the new participation strategy will create real opportunities for socially excluded groups such as indigenous and Afro-descendant populations, to give them greater say in national planning and development policy formulation.

Reducing social inequality and poverty in the region is of the highest priority to Norway as a member of the IDB. Over the years, we have actively supported the Bank's efforts to reduce gender inequality and social exclusion. Accordingly, we warmly welcome the development of an Operational Policy for Indigenous Peoples that is consistent with the institutional strategic framework that is being implemented and that will bring the Bank into line with other multilateral development banks. The new policy should be closely linked to the Action Plan to Combat Social Exclusion and focus on human rights.

We are working with the Bank on various fronts to achieve more equitable and inclusive economic and social development in the region. The joint project on fiscal reform in Central America addresses the regressive effects of taxation in the region and targets tax efficiency as a redistributive mechanism for reducing inequality and poverty. Our joint efforts with the OAS and the IDEA on political parties in Central America are concentrating on ways in which political parties can become a more effective tool in expressing the will of the people, with the involvement of political leaders, in order to instill a sense of ownership of this agenda. We are impressed at the progress that has been made in placing the issue of ethics on the regional development agenda and we note with satisfaction our fruitful cooperation in this regard. The wide response from governments, the private sector, and civil society in Latin America has been unexpected but most welcome. The keen interest this agenda evinced shows that people are increasingly seeking a path to social justice and poverty reduction based on ethics and values. Human rights and the fight against corruption are elements that we would like to broach in the next phase of the Initiative on Ethics and Development.

The IDB is a key development institution in the region. In seeking the objectives we all share to attain the Millennium Development Goals in Latin America and the Caribbean, we are committed to continuing to work with the Bank to reduce poverty and social inequality.

Macroeconomic stability in a given country is a necessary but not sufficient condition for stable, sustainable economic growth and successful integration into international markets.

In some Latin American countries, however, macroeconomic stability has been achieved at the cost of economic growth. This not only jeopardizes the stability attained, but has called into question the legitimacy and credibility of responsible management by various economy ministers from the region. A review of these experiences and the extensive related literature mandates that these processes be reconsidered and that actions and methodological concepts be redefined with a view to ensuring that stability is predicated on growth rather than stagnation.

To this end, in early 2003 the National Government of Ecuador defined its major economic objectives to be "the stabilization of the economy, in a manner consistent with sustained economic growth in the medium and long term and supported by improved competitiveness, job creation, and the sustainability of public finances, managed in such a way as to reduce poverty and enhance the social well-being of the population."

In a number of respects, this constituted an abrupt departure from practice in a fiscal year marked by austerity and prudence in public spending and compliance with agreements reached with the International Monetary Fund (IMF) when negotiating a stand-by arrangement. It also clashes with a social reality impoverished by radical inequities and serious gaps in basic infrastructure.

In one way or another, this is a contradiction to which we have all contributed and for which we all bear some responsibility, and I refer not only to domestic policymakers but also to the multilateral organizations that have been with us under various arrangements during the past 20 or 30 years. It is somewhat reassuring to read the "self-appraisals" of the IMF and the IDB in which this view is stated quite clearly.

But progress has in fact been made, including significant progress in all spheres of fiscal management. On the revenue side, there have been structural changes in the tax and customs areas; on the expenditure side, nearly all the countries in the region now have fiscal accountability laws.

In their more substantive aspects, these laws set limits on growth of expenditure and on country borrowing levels; they also include text relating to transparency and hence to the information flows required for transparency. This is one of the most important fiscal policy transformations of the past decade.

In a number of countries, reference is being made to the need for a "sustainable primary surplus." In the Andean region, this concept has been discussed in the context of macroeconomic convergence programs, in conjunction with the importance of fiscal convergence.

This is an appropriate juncture to raise a new matter, i.e., the primary deficit and the "procyclical or countercyclical" nature of fiscal policy.

Clearly, the responsibilities of economic and fiscal policymakers include dampening the extreme swings of the economic cycle. The main tool available for doing this is the national budget: its revenue side; its expenditure side; and its financing. This all sounds well and good, since there is an identified objective and various tools available for attaining that objective. However, every economy minister knows full well that the real economy does not work that way, in part because some components of the budget are inflexible.

All incoming economy ministers must face the reality of a rigid national budget, that includes preexisting allocations on both the revenue and expenditure sides, compounded by various nondiscretionary components of expenditure. Once such obligations—most of which have legislative or even constitutional backing—are added to financial and wage commitments, the scope for addressing contingencies or redefining fiscal policy is greatly narrowed if not eliminated altogether.

Major efforts are being made to enhance the quality of expenditure; sweeping reforms have been launched to rationalize expansion of the public sector wage bill; discussions have been initiated with respect to transferring responsibilities and accountability; complete databases are being built on public expenditure by section. However, all these reforms require time, legitimacy, and sound governance, and are certainly influenced by the role of the political economy in economic policy actions.

Ceilings on expenditure growth, sustainable primary surpluses, budget inflexibility, and macroeconomic adjustment programs combine to form a genuinely complicated maze for those in charge of fiscal management. This is all the more true when viewed from the standpoint of legitimate social demands associated with poverty and social inequalities.

Accordingly, a new methodology is needed for recording public investment when calculating the primary surplus. This applies in particular to investment expenditure financed by multilateral institutions.

Fiscal policy in general needs to be conceived within a methodological framework in which the application of a set of policy measures is related to the pursuit of economic objectives in terms of inflation, economic growth, and poverty reduction.

Fiscal adjustment targets should not force reductions that affect public investments known to have critical linkages, as this would limit the country's economic and social development possibilities by precluding the implementation of major development projects. Cuts in expenditure on productive investment and essential maintenance operations are procyclical, and consequently are prejudicial to economic growth; they are also highly regressive, as they affect the most vulnerable social groups.

Public investment in high-impact projects that enjoy positive synergy with private investment and enhance the efficiency of social expenditure should be recorded separately under the methodology. This is especially true given the current rapid pace of discussions on trade integration and liberalization.

In Ecuador, financing from multilateral organizations has made it possible to carry out development projects that have furthered the initiative to integrate regional infrastructure in the transportation, energy, and telecommunications sectors.

For 2004, economic growth in Ecuador is projected to be substantial, on the order of 6 percent, thanks mainly to the oil sector, which is estimated to be expanding at real growth rates in excess of 20 percent. As regards inflation, the trends being observed clearly indicate convergence toward international levels. Although the change in the monetary system has been an important instrument buttressing this process, the firmness with which fiscal policy has been conducted may well constitute the most important explanatory vector. Inflation for 2003 was 6.07 percent on an annual basis; for 2004, average inflation is forecast at about 3.0 percent annually.

With regard to meeting the fiscal targets set in the macroeconomic program, we hope to achieve overall and primary surpluses ranging from 1.8 to 2.0 percent of GDP and 5.0 to 5.5 percent of GDP, respectively.

Noteworthy as well is the substantial rebound in the value of exports. While this is without a doubt attributable to the rise in oil prices, it should also be noted that nontraditional exports showed a significant rising trend throughout the past year. At the same time, imports slowed, in particular those intended for final household consumption, thereby confirming the favorable structural change observed in the sources of economic growth.

It is important that we initiate a joint regional effort, with support from the multilateral development institutions, aimed at adjusting the methodology for recording some kinds of public investment so that they are not included in the computation of the primary surplus, addressing at the same time the urgent need to achieve greater flexibility in favor of a more active fiscal policy.

We must never lose sight of the close connection between the necessary macroeconomic discipline and the political and social realities of our countries. Extreme stances benefit no one, and the search for perfection often blinds us to sound, workable options. Latin America is plagued by cases in which there is a disconnect between macroeconomic performance and local social and political realities.

Turning to the challenges facing the Bank, I wish to reiterate our full support for two topics of particular interest to the countries of the region in terms of making the Bank's participation in poverty alleviation more effective. The first issue is the institutional efforts to strengthen approaches to the private sector, in both the regulatory and the financial spheres. The second concerns lending instruments that could contribute to and supplement efforts to adapt the use of resources to the needs of borrowing countries.

The Ecuadorian economy is in the midst of a gradual transformation that will foster private sector participation in various spheres, both in infrastructure and in services. We will strive to ensure that the various objectives proposed on the basis of the work of the External Review Group chaired by Pedro Pablo Kuczynski and, thereafter, by the Executive Vice President and the Board, take concrete form before the Okinawa Annual Meeting.

Since October 2003, the Bank has been operating under a new capital adequacy framework that has made it possible to demonstrate its financial soundness. We feel that this should allow for a new financing arrangement capable of maximizing the return on each dollar lent to the region. Doing so will require defining a number of criteria aimed at measuring ever more accurately the results of Bank activities in the region.

The IDB has played an important role in support of the Ecuadorian government so as to avert any scenarios involving political deterioration.

We applaud the fact that the Inter-American Development Bank has set several targets for incorporating a number of "best practices" into its work with the countries, with a view to ensuring that the Millennium Development Goals are met in each of its members.

Finally, I would like to report that the Republic of Ecuador has offered to host the Annual Meeting of the Boards of Governors of the Inter-American Development Bank and Inter-American Investment Corporation in 2009. The Bank will shortly begin the steps for complying with the relevant procedures for making the respective presentation at the next meeting of the Board of Governors.

It is an honor for us to participate in this meeting of the Boards of Governors in Peru. We thank the Peruvian government for its invitation and the people of Peru for their warm welcome. We hope to be able to make a contribution to the matters that bring us here today.

On this occasion, I would like to offer a few remarks on the international economic situation, what we have learned about macroeconomic policies in a globalizing economy, and our thoughts about the tasks and challenges that lie ahead for the institutions that have brought us together for this gathering.

The world economy is doing better than it has in the last four or five years, with growth forecasts on the order of 4 percent this year. This development is crucial for the region's economies since it offers promise of higher growth that will permit us to increase public investment and social investments. We can expect as well that the region's private sector will have more access to financing on reasonable terms. It is also foreseeable that foreign direct private investment will increase, with the ensuing benefits in terms of growth and the incorporation of new technologies and knowledge.

Business Cycle Challenges in Emerging Economies

Now that some breathing room appears to be opening after a chapter of crisis, this is a good time to reflect about what we can do or change, based on what we have learned in recent years.

Let me begin by laying out two factors that condition the analysis.

First, most of the emerging economies are subject to commodity shocks and financial shocks.

Second, most of the emerging economies have investment opportunities that exceed their internal savings and will tend to be net importers of capital. Therefore, if financing is available, we will run a current account deficit and build up foreign debt.

The main point I would like to underscore is that the cycles of demand for commodities and the associated price cycles alter the perception of the credit risk posed by our economies. The result is procyclical behavior by investors and lenders, be they public or private, local or foreign.

When demand for commodities and commodity prices fall, our currencies are devalued. This increases the debt-to-GDP ratio and the debt-to-exports ratio, reduces domestic asset values—particularly when measured in dollars—and heightens the credit risk from the standpoint of foreign investors and rating agencies.

This sequence of events is fueled and sharpened in three situations:

- First, when exchange rates are relatively rigid;
- Second, when fiscal policy acts procyclically;
- The third element that influences procyclical behavior is private debt. We all know from experience that the private sector—borrowers and lenders—also behaves procyclically. The 1982 crisis in Chile and the 1997 upheaval in Asian markets are clear examples of private sector overlending and overinvestment. That is why the quality and depth of the supervision of portfolio risk in financial institutions is so important for macroeconomic stability.

It has been concluded in many quarters that part of the solution to the problem of cycles is exchange flexibility, but exchange rates themselves can also be procyclical.

Our approach to this problem has been to promote exchange flexibility coupled with the development of futures markets. But we must acknowledge that maintaining a flexible exchange rate policy, implementing a countercyclical fiscal policy, strengthening supervision of the financial system, and developing liquid and deep futures markets require a large reserve of institutional capital, which is often absent.

Public and private international lenders need to find a way of limiting their credits to reasonable amounts in the upswing of the cycle. This is not easy, because it is always easier to lend to someone who has money.

It is also necessary to find a way to keep credit from shrinking during business cycle downswings. From the standpoint of the banks, the quality of debtors has deteriorated and from the standpoint of international lending agencies "there is no room to lend" except to partially refinance debt taken on during the upswing, because there are no counterpart funds.

Yet another phenomenon is "contagion," where private creditors, based on their risk indicators, stop lending and even withdraw funds from all the countries in a given category, regardless of the underlying situation or the sustainability of their fiscal position.

The observed or cyclical fiscal balance, like that of companies, is not what matters when it comes to assessing true credit risk: attention should focus on the underlying balance, corrected for distortions of the cycle. In recent years, Chile has anchored its fiscal policy in a rule that permits public finances to act countercyclically. We have also strengthened institutions in order to avoid volatility in domestic credit; thus were we able to prevent the external crisis from turning into a domestic recession. Even so, the pace of growth during this period has been half the 1990s average, which indicates that other players also have to equip themselves to avoid procyclical behavior.

We are not convinced that commercial and official creditors have done all they can to reduce their procyclical behavior. We are concerned over agreements such as Basel II, the abandonment of efforts to create contingent lines of credit, and the credit policies of IFIs that limit public investment during cycle downswings, all of which can fuel the commodity cycle.

Combating cycle volatility in Latin American and Caribbean economies is not just an economic imperative, it is also a political one, with short-term and long-range implications.

The depth of business cycles in Latin America and the Caribbean erodes confidence among outside observers and creates frustration for ordinary people who suffer the consequences at home. Deep business cycles are fertile ground for prejudices and populism, that look to easy explanations for complex problems and contribute nothing to their solution.

But deep business cycles are neither a curse nor an endemic feature of our nations. In this region, we have the example of countries like Chile and our host, Peru, that have successfully weathered this latest international crisis.

The Global Economic Outlook

Today there are clear signs that the world economy is recovering, as indicated by the global growth estimates I cited at the outset. However, there are some clouds on the horizon that still are cause for concern. I am referring mainly to the problems that arise from the twin deficits of the world's largest economy, imbalances that fundamentally stem from U.S. fiscal policy. I have two comments to make in this regard. The first is that it will be necessary to adjust this budget in a timely, decisive and systematic manner to avoid excessive pressure on interest rates in the U.S. economy. The second is that as the United States adjusts its level of spending, it will be necessary for other economies to help propel the global economy. It is therefore comforting to observe the recovery in Japan, which is beginning to be accompanied by a recovery in domestic investment. China's growth continues to be spectacular. It has become a major importer of raw materials, manufactures and services, all of which helps to explain the stronger prices for our raw materials.

Europe will, of course, have an important role to play in the process of realigning the world economy. We hope that the expectations of a new reduction in European Central Bank interest rates are borne out and that the governments resolutely address the new structural challenges, which will boost growth rates in the medium term.

International financial conditions are undoubtedly improving. There are positive signs in Asia and a renewal of flows into the economies of Eastern Europe.

Although our region will grow more this year, we have the capacity to absorb much larger flows of external investment and savings, which would allow us to help sustain international demand and growth rates. From our standpoint, it does not make a lot of sense that some of the region's economies have been forced by circumstances to accommodate huge current account surpluses when they should be absorbing external savings and investing in their economic and social development.

But let us remember that the current phase of expansion will not last forever. We should seize the moment to promote initiatives, reforms and policies that will help us reduce our region's economic volatility. Otherwise, development policy and the eradication of poverty and inequity—the real work of public policy—will continue to be subordinated to the short-term imperative of restoring macroeconomic balances.

The Role of the IDB and the Inter-American Investment Corporation

Like other Governors, on earlier occasions we have reiterated that the multilateral development banks should redouble their efforts to attenuate the procyclical effect of their lending. With all due recognition of the IDB's efforts in this regard, we believe that it should help our countries build economic institutions that allow countercyclical policies to be sustainably applied, this being undoubtedly one of the stiffest challenges we must tackle as a region. In addition, the Bank's lending instruments should be fine-tuned and its analytical expertise and institutional credibility brought to bear to support the development of our capital markets and thereby attenuate our economies'oversensitivity to external shocks. One acknowledged example has been the successful design of an infrastructure guarantee program that has enabled private investors to reduce their exchange risk. We would like to continue prioritizing this work agenda, which should lead to the creation of innovative financial products to support the region's needs.

One thing to remember here is that the current lending framework reflects the consensus and commitment of the IDB's shareholders to establish clear ground rules in lending to the region. Another feature of the consensus is a work agenda in such key areas as development effectiveness and the new lending instruments that seek to increase the impact of Bank action. And, again, the Board of Executive Directors and Management need to provide pertinent information on the operation of this lending framework.

We strongly support the Bank's work to step up its work with the private sector. The time has come to act and we urge the Board and Management to move ahead quickly with this agenda.

We reaffirm the important role that the MIF has played in the region's development and stand ready to support the replenishment process. We hope that new partners will join this important initiative in this next stage.

Lastly, we support the admission of new Asian members to the IDB Group. We believe that countries such as Korea and China can contribute greatly to the region's development and we hope to see them participate in the next year's meeting in Okinawa, Japan.

First of all, I should like to express my heartfelt appreciation to the Government of Peru and the local authorities for their very warm welcome and for their excellent organization of this Annual Meeting of the Board of Governors of the Inter-American Development Bank here in Lima.

I would like to begin by highlighting the positive outlook for the region. Although the first few months of 2003 were marked by uncertainty on the international scene, in the second half of the year the world economic situation began to improve substantially and growth to pick up, leaving behind the specter of recession in the region.

A growth rate of 1.5 percent in an environment with moderate inflation and a strengthening of fiscal and exchange policies warrant congratulations. In addition, intraregional trade has partially recovered, and we are pleased to note that for the first time in recent decades Latin America posted a positive current account balance of US$6 billion.

The economies of Latin America are now accessing financial markets at a much lower cost. Sovereign bond issues are recovering and risk is lower in most countries, helping to stem the financial outflows of the past few years. The increase in net capital inflows (US$25.8 billion in 2003, compared with US$10.6 billion in 2002) reflects greater confidence in the region on the part of the financial community.

Projected growth for the region as a whole in 2004 is encouraging: a rate of between 3.5 percent and 4 percent is expected, and for the first time since 1997, no negative growth is projected for any country in the region.

This year, the uncertainties surrounding the economies of Argentina and Brazil have dissipated to some extent. Argentina posted robust growth nearing 8 percent in 2003, after the 10.8 percent drop the previous year. We are hopeful that the measures implemented to maintain macroeconomic stability and ensure the conditions necessary for investment as the engine of growth will indeed lead to the projected growth rate of 4.5 percent for 2004.

In Brazil, recovery of domestic demand and restored foreign investor confidence make us optimistic about this fiscal year, in which growth may reach 4 percent.

However, we are concerned that per capita gross domestic product in Latin America and the Caribbean remains below 1997 levels, that the unemployment rate remains above 10 percent, and that poverty plagues 44.4 percent of the population, or over 225 million people.

Accordingly, in our opinion, it is particularly important to stress that the region should not fail to take advantage of these positive developments to address its weaknesses and reduce its vulnerability to external factors, thereby increasing the standard of living in the region and eradicating poverty.

To do so, in addition to favorable external conditions, the economies of Latin America and the Caribbean must redouble their efforts to implement consistent macroeconomic policies—giving priority to fiscal consolidation policies—and structural reforms that will help remedy old weaknesses.

Of particular importance will be promoting conditions for foreign and domestic capital to be used for investment in production and developing export potential by strengthening regional integration processes and better penetration of world markets.

In this connection, it is crucial to establish an enabling environment for investment, which is the engine of growth and of opportunity for stable employment.

Moreover, the region must implement the necessary policy and administrative reforms that will lead to a regulatory system and institutional framework that are more efficient, transparent, and accountable. These will ultimately be the determining factors for investor confidence and growth.

The IDB has clearly demonstrated its commitment to these objectives. We therefore very much appreciate the Bank's efforts to make new lending instruments available to the countries in the region. In addition to enhancing its capacity to meet the new needs of its members, the Bank has been adapting its procedures to international practices, by updating its risk management methodology in keeping with a new model and capital adequacy policy.

Bank lending surged with a 38-percent increase in disbursements in 2003. However, the decrease in investment lending should be addressed.

Accordingly, and to prevent fiscal consolidation from hampering public investment, Spain has been supporting the development and implementation of formulas to allow government accounting that includes investments made by public or private entities in order to remove an effective obstacle to government investment in infrastructure, while retaining the necessary fiscal discipline and budget transparency.

We are also pleased about the recent approval of the private sector development strategy, which should be implemented without delay. We consider it equally important to move forward in the reform of the Bank's organizational structure.

To this end, a specific program of structural reform measures should be proposed for approval before the next Annual Meeting in Okinawa.

We are very pleased with the success of the Inter-American Investment Corporation and the Multilateral Investment Fund (MIF) this year.

Special mention should be made of the MIF for its major contribution to the development, innovation, and competitiveness of the private sector, particularly small and medium-sized enterprises. These successes will now need to be consolidated with the necessary policies and reforms, including replenishment of the MIF.

Spain wishes to reaffirm its commitment to Latin America and the Caribbean once again at this meeting. In recent years we have become the second largest investor country, with a net investment of over 70 billion euros in the past decade.

Although recent figures show a slight slowdown in Spanish investment flows, Spanish investment in Latin America and the Caribbean is a long-term strategy. The companies will not leave as long as they can restructure their positions in the region, and will remain there to help foster economic growth.

From an institutional perspective, the activities being carried out by the Spanish government reflect Spain's long-term commitment in the region. I would like to point out that bilateral concessional lending channeled through the lending programs managed by the Ministry of Economic Affairs has totaled over 2.2 billion euros in the past few years.

Spain has also made special efforts for bilateral debt relief for IDB member countries. The debt-for-investment swap programs have helped transform debt service into project financing for development and mitigation of natural disasters.

Spain has thus provided more than 800 million euros in debt relief to Latin American and Caribbean countries in recent years.

In addition, we have helped provide multilateral debt relief for Bolivia and Nicaragua in the amount of US$65 million through such institutions as the Andean Development Corporation (CAF) in the case of Bolivia

(US$25 million) and the Central American Bank for Economic Integration (CABEI) in the case of Nicaragua (US$40 million).

In this connection, recently we have strengthened our cooperation with multilateral financial institutions in the region.

First, we joined the Andean Development Corporation as its first nonregional partner and have been a full-fledged member since January 2003.

Second, we joined CABEI at the beginning of the month, during the visit to Spain of the Central American presidents, and have subscribed 10 percent of CABEI shares.

Conclusions

In conclusion, I would first like to highlight the opportunity to take advantage of the current favorable economic situation that is just developing, to deepen the necessary reforms and promote integration of the region into the international economy. These elements of economic policy have proven key to achieving sustained growth.

This is also the time to develop strong institutions that will help integrate the countries in the region into the international economy and thereby increase their flexibility and adaptability to a changing environment, thus reducing their vulnerability.

The IDB's advisory role in this process is more important now than ever. Its contribution is key to promoting dialogue among the public sector, private sector, and civil society and thus building the internal consensus necessary for progress.

Similarly, the Bank's capacity to defend common interests in the region in multilateral trade negotiations should help address the challenges of the coming months. And Bank support for these economies should contribute to greater investor confidence.

Lastly, I would like to highlight Spain's firm commitment to the region and to the institution headed by Enrique Iglesias at this decisive juncture, to meet the challenge of achieving strong growth that will benefit all. I wish us all the best of luck in this endeavor.

ADDRESS BY MR. OWEN ARTHUR, GOVERNOR FOR BARBADOS, ON BEHALF OF THE ENGLISH-SPEAKING COUNTRIES OF THE CARIBBEAN

I have the honor today to address this joint Annual Meeting on behalf of the five Caribbean nations that are members of the Caribbean Constituency—The Bahamas, Guyana, Jamaica, Trinidad and Tobago, and my own country, Barbados. I am pleased to convey our delegations' appreciation to the Government of Peru and the city of Lima for the hospitality extended to us in this city that is so unique in our Hemisphere. I must also compliment the Management and staff of the Bank for the excellent arrangements they have made for this meeting.

Chair, we congratulate you on your election and your assumption of responsibility for the Bank over the next year, which presents new challenges in accelerating the growth of our economies. Our Constituency also thanks the Governor for Italy for the innovative developments put in place during his chairmanship, and in particular for the greater emphasis placed on private sector operations.

Our fears concerning the adverse impact of the international economy last year on countries of the Constituency did not materialize. We saw the beginnings of a recovery, especially in tourism. The signs are that these trends will strengthen and become more broad-based. Nevertheless, the foundations remain subject to external vulnerabilities, both man-made and natural.

Most Caribbean countries, like others in this region, shared in the incipient recovery. The year ended with accelerated growth rates in real terms in The Bahamas, Barbados, Jamaica, and Trinidad and Tobago, while there was some deceleration in Guyana. In Jamaica, the authorities continue to have as their main focus the improvement of the fiscal and debt situation. The objective is to have a balanced budget by the end of fiscal year 2005–06.

In the region, monetary and budgetary policies continued to be prudently managed, with investments concentrated in tourism and energy, and on poverty reduction programs. We recognize that the Millennium Development Goals represent minimum standards, but we have set ourselves national goals in some areas that exceed these. The task ahead also includes structural diversification, achieving international competitiveness, stimulating entrepreneurship, and ensuring that the benefits of growth are spread throughout society. These are areas for which we would welcome greater assistance from the IDB Group.

A new Country Strategy for The Bahamas covering the period 2003–07 was approved by the Board of Directors on March 10, 2004. The principal objective of the strategy will be to support the economic and social development of the country by helping the government, the private sector, and civil society to address a broad range of development challenges.

A new Country Strategy is being drafted for Barbados and is expected to be approved in the latter half of this year.

During the past year, Guyana achieved completion point under the Enhanced HIPC Initiative and became eligible for debt relief of US$64 million in net present value terms from the IDB. A total of 11 technical cooperation projects were completed in 2003, and four new ones were approved with a value of US$1.8 million.

In Jamaica, the fiscal constraints resulted in a reduction in the government's public sector investment program and this affected the pace of implementation of projects. The government and Bank officials have undertaken an extensive review of the portfolio consistent with the fiscal objectives of the government.

Trinidad and Tobago currently has a portfolio with an average age of three and a half years, including a Trade Sector Support Programme, the first of its kind in the English-speaking Caribbean. A new Country Strategy is currently being prepared and is expected to be approved during the latter part of this year.

At the regional level, the Bank has provided assistance for several aspects of the Caribbean Single Market and Economy (CSME), including for external trade negotiations in which the CARICOM is involved, as well as assistance to the Caribbean Development Bank. As the region strives to position itself more competitively in the world economy, there will be a continuing need for such assistance, in particular for the preparatory and implementation phases of the FTAA, the WTO multilateral trade negotiations, and the CSME. We should like to see the Bank moving forward in the near future to an updated regional program that would take account of evolving priorities.

Approvals for the Caribbean Constituency for 2003, including private sector lending, totaled US$43.5 million for four loans and represented 0.64 percent of total approvals for the region. In dollar terms, this amount is considerably below approvals for the year 2002 when approvals to the Constituency total US$144.4 million for seven loans and represented 3.2 percent of the US$4.5 billion approvals. Also, during 2003 the Constituency recorded a negative net resource flow of US$229.1 million, reversing the positive net flow of US$20.8 million it had during the previous year. While we welcome the Bank's first loan to our private sector, public sector lending reached a low of US$13 million. We believe that these figures highlight the fact that there is considerable room for the Bank and the Constituency to work together to bring about more favorable outcomes.

We are pleased to see the implementation of the capital adequacy framework that was approved by the Board of Executive Directors last year. Its introduction is very timely as it will not only strengthen confidence in capital markets, but we, the shareholders and borrowers, will be able to see precisely the link between loan charges and the Bank's profitability.

We fully support and will continue to contribute to the Bank's efforts to develop new lending instruments. We expect these instruments to respond more closely to the particular needs of the borrowing countries. They should have a positive measurable impact on the lives of our citizens, as reflected in increased income and improved standards of living.

We recognize that one of the most effective means of increasing incomes is through the development of our private sector. To this end, the countries of the Caribbean Constituency have been developing incentive programs for the private sector. For example, in Barbados private sector-generated growth is being facilitated, among other ways, by placing a cap on expenditures for government-owned entities involved in quasi-commercial activities.

We therefore support the initiatives being taken to foster the kind of environment that is conducive to private sector development, and note that Trinidad and Tobago was one of the first countries signatory to the Business Enhancement Project of the IDB. We welcome the Bank's continued intervention in this area in the other countries in the Constituency.

We applaud the increased focus of the IDB Group on private sector activities and encourage a merger of its private sector operations. This should be done in a way that would be beneficial to both the private sector and the public sector operations in the region. Deliberations on this initiative should be concluded in the near future.

We are pleased that for the first time since the creation of the Private Sector Department of the Bank, a country in our Constituency has been able to access these resources, in the form of a loan for US$30 million to a Jamaican enterprise. We also note that the Inter-American Investment Corporation also approved three loans to the Constituency for a total of US$23 million, the first time in four years resources were approved directly to the Constituency. One of these loans went to a Barbadian company and will be used for onlending to small and medium-sized enterprises, including those of Trinidad and Tobago and Guyana. The two other loans were made to enterprises in Jamaica, a tourism project and a regional financial intermediary. It is noteworthy that funds made available to the Caribbean private sector from the IDB Group in 2003 were substantially in excess of those to the public sector. We expect this positive trend in lending to our private sector to continue.

Coincidentally, the MIF, which has normally been the most responsive to the Constituency, reduced its resources to our countries in 2003. Given this window's mandate to strengthen the environment for private sector development, we strongly support the replenishment of its resources and urge those members of the Bank who are not donors to the MIF, to lend their support to this very effective operation.

We note that interim arrangements have been made for the Office of Development Effectiveness, and we urge that permanent arrangements be put in place in the near future. We believe that improving the effec-tiveness of development interventions in a country is not only the responsibility of the Bank, but also that of the country. We look forward, therefore, to the Bank's continued assistance in increasing our institutional capacity to effectively prepare and monitor projects.

We note that the Bank currently has under consideration the disposal of shares that have recently become available. We expect that this process will be completed in the near future.

In closing, the member countries of the Caribbean Constituency express their continued appreciation to the IDB Group and encourage the Board of Executive Directors and staff to pursue their innovations in responding more effectively to the development agenda of the member countries.

I. INTRODUCTION

It is a great pleasure for me to address the Forty-fifth Annual Meeting of the Inter-American Development Bank and the Nineteenth Annual Meeting of the Inter-American Investment Corporation. On behalf of the Government of Japan, I would like to express our gratitude to our hosts, the Government of Peru and the people of Lima, for their warm hospitality.

Japan's economy is on a steady track to recovery. It is supported primarily by an increase in capital investments and exports to Asia. To transform this momentum into a sustainable growth against the severe fiscal situation, our government will continue to implement the structural reform agenda, such as pension reform, reform of central and local governments, postal privatization, Japan highway privatization, and resolution of the nonperforming loans problem. We will also collaborate with the Bank of Japan to overcome deflation as early as possible.

II. ECONOMIC ISSUES IN THE REGION

Now to the Latin American and Caribbean economies.

Helped by the recovery of industrial economies and the rising prices of primary commodities, the region's economy, which had remained stagnant since the 1998 financial crisis, has finally bottomed out, and we are now witnessing some positive signs of recovery.

Even in the face of adversity, some countries implement sound economic management. The GDP growth rate for the region's economy on the whole has turned positive, and is expected to reach almost 4 percent this year. Foreign capital inflows have also started to pick up, reversing the trend of a constant decline triggered by the financial crisis. It should be commended, in particular, that Brazil and other crisis countries are making steady efforts to promote reform with the cooperation of the IDB and other international organizations. I would also like to highlight that Japan and Mexico reached agreements in substance on major elements of the Agreement between Japan and the United Mexican States for the Strengthening of the Economic Partnership.

Having said that, however, I must point out that while many countries in this region enjoy higher income levels than Asia, income disparity has not improved. The region has come only halfway to overcoming vulnerability in financial intermediation and administrative inefficiency, and to improve enabling environments for business to desirable levels.

As for Argentina, in particular, while I welcome the recent signs of economic recovery, I believe it is indispensable to restore the confidence of international capital markets by resolving its external debt issue as soon as possible in order to achieve sustainable growth.

III. IDB'S CHALLENGES

Against such a backdrop, the IDB must redress income disparity and develop enabling environments for business in the region. To take on these challenges both efficiently and effectively, I believe it is essential for the IDB to pursue its own reform in the following three areas: first, the Private Sector Development Policy; second, result-based management; and third, strengthened financial standing and improved accountability.

Private Sector Development Policy

Many of the IDB borrowers are middle-income countries. In the long run, the key to their economic growth lies in private sector lending, or public-private sector partnerships, and the development of enabling environments for business. These are not something the Private Sector Department of the Bank and the IIC alone should address.

Rather, it is essential for the entire IDB Group, including the regional departments, to maximize their synergy based on a comprehensive private sector strategy, with strengthening competitiveness and improving enabling environment as the primary objectives of IDB operations.

In this context, I welcome the recently formulated Private Sector Development Strategy (PSDS). It marks the first step in the right direction. I would like to take this opportunity to urge the IDB to promptly detail its action plan and country strategies based on the Private Sector Development Strategy, and translate them into action.

In the wake of all this, there is a move to replenish its capital for the Multilateral Investment Fund (MIF). While MIF is a unique fund with a mandate to support micro and small enterprise, we must first give detailed shape to the Private Sector Development Strategy of the entire IDB Group and ensure participation of many donors before we negotiate a capital increase for the MIF. I hope all parties concerned will continue an active discussion to this end.

With regard to the task of redressing income disparity, in addition to the aforementioned support of micro and small enterprise, I think it is essential for the IDB to secure a social safety net, while continuing to raise the efficiency of social services delivery. For this objective, capacity building of civil servants including local government is indispensable.

Also, I understand the IDB is about to conduct a review of the New Lending Framework. In reviewing the framework, particularly as for the Policy-Based Lending, we need to evaluate the development effectiveness of past PBLs and cautiously examine its impact on the Bank's overall financial position.

Result-based Management

At the IDB, implementation of the Development Effectiveness Agenda, first announced at the Monterrey Summit and reaffirmed at a recent meeting in Marrakesh, has only just begun.

At this stage, it is essential for the IDB to pursue results-oriented policies by devising measurable monitoring indicators, while identifying the result chain between IDB activity in each recipient country and its development effectiveness at every stage of the lending operation—from design to implementation and evaluation—not to mention Country Assistance Strategies. To implement all this, sharing borrowers' development plans with other multilateral development banks and bilateral donors will be indispensable. I hope the IDB will formulate a more detailed action plan, by activating the Development Effectiveness Office established last year.

Also, for recipient countries, it is essential to prepare the data needed to measure the effectiveness of their development plans. That's why the capacity-building effort in recipient countries is vital.

Donors, on the other hand, should also spare no effort to support such activity by recipient countries. For its part, Japan will continue to support the program for the Improvement of Surveys and Measurement of Living Conditions in Latin America and the Caribbean.

Strengthened Financial Position and Improved Accountability

The Bank's fiftieth anniversary is only five years ahead. To make a further leap forward, the IDB needs to listen to the opinions of external stakeholders and strengthened governance to use those opinions as the food for thought for its own capacity building.

In this regard, the new capital adequacy policy the IDB adopted last year is commendable as it contributes to the Bank's strengthened financial position, while clarifying the responsibilities of both shareholders and debtors. Likewise, the new Information Disclosure Policy, launched this year, is an essential step toward increased accountability of the Bank, though there is room for further improvements.

Regarding enhancements to the Independent Investigation Mechanism that are currently under study, I strongly hope that the proposal will lead to the establishment of a creditable mechanism that can match up to the equivalent mechanisms at other MDBs.

IV. INVITATION TO OKINAWA (CONCLUSION)

In closing, I would like to extend to my fellow Governors an invitation to our next meeting in Okinawa. Japan and the Latin America and Caribbean region have built up a trusting relationship through trade and investments over the centuries. Our economic ties, however, could never have been this strong without the history of emigration that has lasted over a century. We are proud that 1.5 million Japanese emigrants have crossed the sea to work as a bridge between Japan and this region, while contributing to the economic and social development in the region. At present, over 210,000 emigrants from Okinawa are active in various fields in the Latin America and Caribbean region.

As with Peru, it is blessed with a beautiful natural environment and vivid traditional arts. I am sure a visit to Okinawa will be a memorable experience.

I'm very much looking forward to seeing you again in tropical Okinawa in April next year.

I would like to begin by conveying my regards to all the authorities, delegations and guests here today and expressing our special thanks to the people and Government of Peru.

Unlike the situation last year, this year's meeting is being held in a climate of economic recovery in Latin America and the Caribbean and in the world economy.

After four years of economic depression—the longest and deepest in more than a century—Argentina began to see signs of recovery in mid-2002, which strengthened in 2003 as the gross domestic product grew by 8.7 percent and inflation stood at 3.7 percent.

In the space of 20 months, over 2 million jobs were created, two-thirds of them (1.35 million) new jobs in the private sector and the rest corresponding to emergency job creation programs. The deplorable historical levels of unemployment caused by the crisis are no longer present, but the rate is still high (14.5 percent). One of the cornerstones of our economic policy is to create an additional 2 million jobs.

Higher employment, coupled with targeted social policies and wage increases made possible by greater economic productivity, have brought about a sharp drop in poverty and extreme poverty levels.

One very important aspect of this recovery is that total investment has increased by nearly 50 percent and the incorporation of imported equipment has more than doubled.

On the fiscal front, we have moved from average primary deficits of 2 percent in the 1990s to primary surpluses of 3 percent, including central and provincial government surpluses for the first time in decades.

The financial system, which was virtually wiped out after the collapse of convertibility in December 2001, today has excess liquidity and is enjoying strong recapitalization.

The exchange rate is stable and floats freely, and reserves are being rebuilt. As a result, it has been possible to repay US$7 billion net to international lending agencies (including the IDB) over the past two years.

A crucial step was taken with monetary reunification, whereby the 14 provincial currencies that arose during 2000 and 2001 were reabsorbed.

International circumstances have had both a positive and a negative impact on these developments: positive, thanks to higher prices for our agricultural and energy exports; and negative, owing to weak regional demand triggered by recession, particularly in MERCOSUR, and the consequent marked impact on exports of industrial goods.

Dwindling external financing, the temporary delay in the launch of the economic normalization and recovery program, and the arrangements with the International Monetary Fund (IMF) and other multilateral institutions have also played negatively in this landscape.

The two programs with the IMF—the January 2003 transition program and the three-year arrangement agreed on in September 2003—are expected to consolidate the results obtained under the policy framework established by the authorities without external support.

Projections for 2004 indicate growth on the order of 5.5 percent, with a drop in unemployment, curbed inflation, and further progress in institutional strengthening and social cohesion.

Although significant headway has been made, we realize we must still address a number of key economic and social problems that are the legacy of the past decade's failed policies. We and the international community are all keenly aware of the enormity of the task that lies ahead.

We also know that the fallout from social and political destabilization engendered by impoverishment is even more serious than that generated by high poverty levels.

I would like to refer briefly to the arrangement with the IMF and the negotiations on the portion of the public debt that is in default.

As President Kirchner said in his opening address to Congress last March, this administration did not declare the default, but neither can it evade the situation it has inherited or shirk its responsibilities. It is intent upon bringing the 55 percent of its debt that is today in default back into paying status, but recognizes that the formulas of the past are no longer applicable.

The day after agreement was reached with the IMF in Dubai in September 2003, the government made good on its promise to present a road map for restructuring the debt. One prerequisite for that map was to have an arrangement in place with the IMF that established key parameters for the financing program.

In this regard, the Argentine government has stressed the "single pocket" approach. Not only is Argentina not receiving fresh money from international organizations, it has been making large net payments to those institutions, on the order of US$7 billion in 2002–03 (considering principal and interest). This means that there is less money available to pay private creditors.

Since the debt-restructuring proposal was announced, the Argentine government has pursued the process in good faith, obeying one basic rule: not to promise what is materially impossible to deliver. Since May 20, 2002, we have held 57 consultation meetings with creditors and will continue to do so, as part of a well-defined program.

However, this will be a different restructuring—not just on account of its size and technical complexities, but also because it will be the first one to involve a change in the rules that guide the operation of the international financial system. Unlike the situation in the 1990s and as part of the effort that we share intellectually to counteract the effects of moral hazard, there are no more packages of international public funds to resolve the problems of private bondholders.

This will make such restructurings less market-friendly while simultaneously requiring—in the interest of consistency—that some of the other rules under which the financial market operates also be adapted. The minimum thresholds for restructuring, the terms of the new debt, the treatment of interest arrears, creditor representation, and the resulting nominal debt cannot be the same as they were under multilateral or bilateral rescue packages that used public funds.

Even the pari passu, which we will respect, will have to be reexamined to differentiate between original holders and post-default buyers.

Modifying just one of the rules of the international financial system without adjusting any of the others would be inconsistent, an intellectual error, and a source of conflict and frustration.

Even if there are no "public funds" forthcoming, the international financial community should operate within "public criteria" that focus more on the objective of achieving sustainability than on acceptability.

That said, we continue to be interested in and committed to securing greater market acceptance. Our technical work seeks to strike a balance between Argentina's domestic social and economic objectives and the degree of acceptance.

Argentina hopes to reach an agreement that is sustainable so as not to require subsequent reschedulings, which were frequent in the 1990s and created uncertainty that undermined investment and growth to the detriment of all concerned.

We believe that the fiscal effort built into the current program, which has already yielded an improvement of 5 percent in GDP, is significant by any yardstick and that it will permit growth with social cohesion to be maintained to the benefit of all, including private creditors.

The only way in which we can all win is through recovery and creation of value. By using growth-linked bonds, holders of defaulted bonds will also be able to benefit from the considerable growth potential of our economy.

I will turn now to the IDB.

In 2002, Argentina made net payments to the Bank in the amount of US$1.07 billion, (principal and interest); in 2003 that figure fell to US$325 million. Counting only principal payments and disbursements, the IDB contributed net flows to Argentina for just under US$300 million in 2003. We acknowledge the effort made by the IDB, particularly since not all of the multilateral financial system has been so well disposed.

It is important to reiterate that multilateral organizations should not play a procyclical role. Their function should be countercyclical, making a net contribution to financing development in the medium and long terms.

There are three basic requirements if this is to happen:

- The concept of development (rather than adjustment policies) needs to be returned to center stage;

- Suitable financial instruments must be available that, in addition to providing liquidity, give due consideration to development impact; and

- The IDB's financial soundness must be safeguarded, without resorting to financial and operational criteria that are so restrictive that they end up limiting the IDB's contribution when the region needs it most.

The first step is to make full use of the annual lending capacity of close to US$8 billion that exists today and which was not wholly used in 2002–03.

At the same time, we would like to see the financing caps revised, particularly raising the ceiling for policy-based loans (PBLs). The existing quota of US$1.5 billion a year is low.

Under the current financing framework, the limited use of investment lending in recent years, far below the US$5.15 billion available annually, should be noted.

We note with concern the attempts to subordinate PBLs to formal arrangements with the IMF, when there are no reasons for this—neither by virtue of the nature of the reforms involved nor by virtue of the profile of disbursements and repayments required under such linking.

With regard to the new investment instruments, it is important for sector reform facilities and time-slice operations to be made available as soon as possible.

It is indispensable to continue the work begun by the presidents of Argentina and Brazil to step up investments with high development impact. Efforts to define methods to assure funding for those invest-ments—without artificial accounting restrictions that make it difficult to provide local counterpart funds—must not be allowed to wane.

As for reform of the IDB's private sector activity, Argentina feels strongly that the approved strategy should be implemented and a study undertaken on a possible reorganization. The operations of the Inter-American Investment Corporation and the IDB's private sector window should be made more flexible. Argentina also supports the business climate initiative to mobilize domestic and external saving capacity and channel such savings into productive investments in our countries. Last, the replenishment of the Multilateral Investment Fund resources should be completed, ensuring its linkage with the rest of the Bank's activities.

All these issues should be viewed as an integrated whole. There can be no effective development if we lack an adequate financing framework, with appropriate instruments and effective interventions in the public and private sectors. At the same time, the borrowing member countries are keen to maintain the Bank's recognized financial solvency, but we also believe that overly restrictive financial or operating criteria—that ultimately limit the IDB's contribution at a time when the region needs it most—do not contribute to achieving development objectives. In the final analysis, it is our peoples who bear the fundamental responsibility for whether development and its financing are effective. Also, effective development and attainment of the Millennium Goals, including goal number eight, require the industrial countries to adopt policies that are more consistent with those objectives.

I would like to end my remarks by expressing the gratitude of Argentina and our government for the support received from the Bank's member countries and, in particular, from President Iglesias, who has always backed our country's efforts with enthusiasm, optimism and intelligence, helping in the search for solutions.

More than a supplier of financing, the IDB is essentially a development institution. We are fully convinced that the Bank should focus on the essence of its action, which is to improve living conditions for our people.

While it is true that we have come a long way, it is also true that Argentina and the IDB still have a very full agenda in this regard.

With the support of democratic consensus, responsible economic and social policies designed in and for the country, and the unremitting and constructive work of everyone, we will surely be able to rise to all these challenges.

It is an honor to have this opportunity to participate in the Forty-fifth Annual Meeting of the Governors of the Inter-American Development Bank and Nineteenth Annual Meeting of the Governors of the Inter-American Investment Corporation. I would like to express my appreciation to the Government of Peru for its hospitality and for the warm reception we have received. I am certain that the work of this meeting will go far in strengthening the IDB as a catalyst of economic and social development.

At the last three Annual Meetings, the international environment was marked by a global economic slowdown and volatile international financial markets. In those years, Latin America's economic performance was at its worst in two decades.

Yet this meeting takes place in a promising economic environment. For most countries, economic indicators suggest that the recovery is gaining momentum.

Of particular importance is simultaneous growth in the three major trade blocs: the United States, Europe, and Japan. Greater opportunities for expansion by emerging economies are combining with the outcomes of national policies, to set off a boom in productive activity in the region.

According to the International Monetary Fund, Latin America will achieve 3.6-percent growth in 2004, far outpacing the 2003 figure of 1 percent. Yet the recovery could be transient in several countries without structural reforms to generate internal sources of growth that make our economies less vulnerable to international turmoil.

In Mexico, fiscal and monetary discipline, proactive management of public debt, modernization of the financial system, and institutional strengthening have helped us cope with these hard times and positioned us to benefit from external recovery. I take this opportunity to thank the IDB for the constructive role it has played throughout this process.

The 2004 economic program maintains fiscal discipline. Only that can assure intergenerational welfare, low country risk, manageable public debt, and the ability to fund private sector spending.

Accordingly, Congress approved the Executive Branch's proposal to end the year with a budget deficit no higher than 0.3 percent of GDP, financed internally as during the first three years of this six-year administration.

In terms of financing from abroad, for the first time in modern Mexican history the government has committed to reduce its net foreign debt, repaying US$500 million. This points up our policy of increasing reliance on domestic debt, to make the country less vulnerable to sudden changes in the global economic environment.

External debt management will concentrate on improving the mix, obtaining better terms, and broadening the investor base, especially among those who invest almost exclusively in investment-grade instruments.

In the area of domestic public financing, the amortization profile and yield curve of government securities will be improved. Maturities are already as long as 20 years with nominal fixed-interest instruments. This establishes essential benchmarks for private debt transactions.

More than a borrowing mechanism, then, public debt policy helps to develop the national financial market by strengthening the private sector's role as an engine of development.

The IDB has been a valuable partner in Mexico's effort to strengthen its economic underpinnings. The

Bank has responded quickly to the need for program support in areas ranging from social development to boosting competitiveness. The IDB has evolved over the years to fulfill its mandate increasingly well.

On the subject of the IDB's evolution, 10 years ago Mexico hosted the Annual Meeting in Guadalajara, where the value of the Bank's contribution to the process of economic and social transformation of the region was reaffirmed.

The Guadalajara consensus was later embodied in the agreement on the Eighth Replenishment, and a milestone was reached: recognition of the importance of economic growth with equity as the top development priority and creation of a lending facility to promote private sector development.

This conviction has guided the Bank's actions. We have given it the resources to support poverty reduction, enhance social equity, advance private sector development as a catalyst, strengthen institutions, and foster stability.

Transformation of the region and its environment calls for ongoing review of the framework in which the Bank operates, so that it can live up to the agreements reached in Guadalajara. This should not be surprising. Change becomes the norm for an institution that, like the IDB, adapts and remains effective.

The challenge facing the Bank today is to become more responsive and shift its operations toward meeting the needs of the borrowing member countries, while becoming financially stronger and preserving its high credit rating.

In this regard, we welcome the new capital adequacy policy adopted by the Board of Executive Directors with its robust methodology for measuring risk. Target levels of capital can be set using this new formula, so as to provide protection against a wide range of credit events.

Now I would like to say a few words drawing on the goals I have described here.

We are concerned that IDB financing levels are well below its lending capacity at a time when greater financial resources are needed to strengthen the processes of economic recovery now under way. More flexible and abundant lending instruments need to be considered, to support these processes.

Structural adjustments that foster growth, economic stability, and protection of at-risk groups can be financed within appropriate limits. One noteworthy example is the IDB's support for expanded financial services to rural Mexicans. This operation, signed yesterday, will help to improve the terms on which bank and nonbank financial intermediaries extend credit to rural customers.

We urge the Board of Executive Directors to continue to study the proposed new instruments with Management, considering both their potential contribution to countries' development strategies and their financial viability for the Bank.

The Bank should build its capacity to achieve results and to measure and evaluate the borrowing member countries. This will also facilitate our public accountability.

Accordingly, the Government of Mexico is working with the IDB on a multiyear evaluation method to measure the impact of social programs, enabling us to get the maximum social benefit from each peso spent on the poorest of the poor.

In Guadalajara, we acknowledged the importance of private investment for sustained economic growth. We therefore agreed to introduce loans without sovereign guarantees, so that the private sector would have access to medium- and long-term financing.

Today, we welcome a new, single framework for the three arms of the IDB Group that support private sector development: the Bank, the Inter-American Investment Corporation, and the Multilateral Investment Fund.

In relation to this new strategy, we support the establishment of a temporary high-level coordination body with clear terms of reference, as well as broadening of the sectors in which the Private Sector Department may operate. We suggest that both matters be taken up soon.

Promoting an enabling business climate is another pressing concern. Private investment flourishes where it finds monetary and exchange rate stability, an effective legal and regulatory framework, a competitive tax structure, and a skilled workforce. That being so, a diagnostic assessment must be done of the environment in which the region's private sector operates.

The IDB has repositioned itself to support the private sector in creative ways that take advantage of its installed capacity. But care must be taken to ensure that this does not increase fees or jeopardize financial stability. I am certain that under your leadership, President Iglesias, we will soon identify how the IDB can play a leading role as a development catalyst through such support.

Now I would like to say a few words about the Inter-American Investment Corporation and the Multilateral Investment Fund.

We were pleased to hear of the Corporation's success, along with the progress report on the action plan. It is a sounder institution today, and can take action to increase revenue, diversify its loan portfolio, and reduce its credit risk exposure.

We urge Management and the Corporation's Board of Executive Directors to develop a new business plan that builds on previous efforts.

We also welcome the decision to hold a special meeting on replenishment of the Multilateral Investment Fund. We agree with the conclusions that emerged from the special meeting, and hope that the replenishment takes place within the agreed timeframe.

Ten years after the Guadalajara consensus, the region still faces daunting challenges. Yet the Bank has been able to reinvent itself along the way and help us find ways of achieving sustained economic growth with equity.

Today, unlike 10 years ago, the Bank requires no replenishment. Rather, it must keep working to enhance efficiency, leverage synergies with other institutions, and continue reinventing itself to fulfill its mandate. Without a doubt, its sound financial position provides a firm foundation for new policies.

Once again, it is heartening to see that the Bank maintains its drive and determination to achieve the goal of economic growth with equity.

Like any other institution, the IDB can either become inflexible or imaginatively transform itself. I have no doubt that we will choose the latter.

I, like those who have taken the floor before me, would like to thank the Peruvian government for hosting this year's Annual Meeting in this fascinating country, and the Bank and its staff for the work that has gone into staging the meeting. As you may have guessed from my name, I have ties to this Hemisphere, which makes the pleasure of being here all the greater.

This region, with which the French people feel such a close bond, is emerging from a deep crisis. In 2003 growth here resumed, following 2002 when this was the only emerging region in recession. The upturn can be attributed to sounder domestic policies, and is supported by a more favorable external environment: higher market prices for commodities, exchange rate trends, and the resumption of growth in the region's main trading partners. More concretely, the developments in certain countries are also encouraging. The new political picture in Haiti is inspiring renewed hope. France encourages the Bank to continue its work in that country, as soon as conditions permit, and pledges its efforts to help normalize Haiti's relations with the international community.

In the medium term, raising the potential for growth remains essential for significantly reducing the inequality and poverty afflicting the region, which unfortunately worsened in 2003. There is still a long road ahead in order to achieve the Millennium Development Goals (MDGs). The region, which is dealing with the emergence of new global competitors, continues to be very vulnerable to exogenous shocks.

In a more favorable overall climate, but one where nothing can be taken for granted, the support of the Inter-American Development Bank is essential. I would like to touch upon the three subjects that are the focus of these Annual Meetings, which pursue the common aim of enhancing the Bank's development effectiveness.

Firstly, in Milan the Governors called on the Bank to resolutely engage in the general shift towards enhanced development effectiveness. I would therefore like to acknowledge Mr. Iglesias's firm personal commitment to bringing development effectiveness to the fore at the Bank and in the countries. One of the keys in this regard is a clear analysis of objectives and expected outcomes of investments.

Admittedly, adopting results-based management is no easy task. All the multilateral institutions, all the development agencies, and all the countries face this challenge, which requires first a change in culture. The recently established Office of Development Effectiveness will have to tackle two major challenges. It must drive the implementation of results-based management at the Bank, working closely with the Operations Departments and the Office of Evaluation and Oversight. France endorses the pragmatic approach presented during the meeting of Governors on Saturday, which augurs well for the future. Ownership of this concept by the countries in the region will be key to success. The Bank must therefore help the countries to build capacity and foster partnerships and experience-sharing. The work done in the OECD Development Assistance Committee, which will organize a high-level forum on this topic in Paris in 2005, can be picked up in the region. The IDB has to take the lead on these issues and release the means necessary for the task.

Secondly, making the Bank's lending as effective as possible also depends on tailoring its products and services to the specific needs of the region.

France supports the Bank's innovation efforts, which were undertaken in response to the requests for increased flexibility made in Milan. One such new instrument in the institution's toolkit is the performance-driven loan, for which preestablished objectives must be met, to better reward performance. The discussion of loans to subnational entities without sovereign guarantees is also very encouraging and hopefully will lead quickly to concrete proposals.

Obviously, these new lending instruments must be evaluated by reference to the Bank's financial strength. In 2003, the adoption of a sounder risk management policy made it possible to comfortably lower Bank loan charges.

The idea, then, is not to keep creating new instruments, but to give the countries the best tools for reducing poverty and inequality, in keeping with the Bank's mandate. Its primary mission is not to provide liquidity but to help achieve sustainable development. To that end, evaluation of the results, performance, and impact of fast-disbursing loans must be strengthened. Regrettably, the recourse and use of the new instruments introduced in 2003 have been extremely limited so far.

The Bank must help the countries, as it always has, with investment assistance, guaranteeing social and environmental criteria that benefit everyone in the region. From this standpoint, the continued drop in investment lending is worrisome. Before looking at any further increase in the flexibility of its instruments, the Bank should pause to evaluate the flexibility that is already there.

Macroeconomic stability remains a prerequisite for Bank operations to have the desired impact on reform and investment performance and a lasting impact on poverty. The Bank, together with the other international financial institutions, should do what it can to help address this imperative.

Thirdly, to achieve the Bank's core objective, it has become increasingly clear that the private sector must play its full role in the region. Only better governance, increased security for persons and goods, and the observance of laws will make it possible to achieve sustainable development. It is up to the countries to create the conditions for mobilizing these resources for development, but the Bank can make a decisive contribution. It can and it must engage in ongoing, rigorous dialogue with its member countries. Thirteen countries have already signed a cooperation agreement with the Bank since the Business Climate Initiative was launched in December 2003. The Bank likewise will help these member countries establish a framework of action and an enabling environment for the private sector, which are essential for attracting the capital flows needed for growth, given the region's weak levels of national saving. Local and foreign investors alike want stronger assurances and greater transparency. It is absolutely essential that they be able to count on stable ground rules, because there is global competition for private capital, and investors will go where assurances are firm.

This is the rationale of the IDB Group's Private Sector Development Strategy, which has just been approved and which France supports. The first priority is to integrate country-specific features when defining and programming the Group's private sector activities. The IDB's Country Private Sector Development Strategies must be consistent with the national development strategies.

This strategy also underscores the need for the different arms of the Bank Group to work together to make their private sector interventions as effective as possible. In this regard, I would like to salute the efforts made to tighten that coordination and hope that President Iglesias will very soon be assisted in this area by a high-level official to coordinate the work of the three institutions and pilot, alongside the President, the implementation of the new strategy. The official could also craft proposals regarding the organization of the Group; however, we should not allow ourselves to become bogged down in endless institutional discussions that would bring us back where we started. It is essential for these efforts to quickly translate into better coordination and hence increased effectiveness in the different entities of the Bank Group that work with the private sector.

With respect to the Inter-American Investment Corporation, I have noted that the concerns voiced in Milan over the Corporation's performance have largely been dispelled. Management has clearly implemented its short-term action plan and achieved its first convincing results.

In closing, I would like to commend the Bank Group as a whole for its work and to congratulate you, Mr. President, as well as Bank Group staff, the Executive Directors, and the countries for the progress achieved in 2003. I also would like to reiterate that my country stands ready, as part of its commitment to official development assistance, to participate fully in this work in and with the region. This commitment to development should also be backed by an innovative approach to lending modalities. As you know, since some of you will be attending, next week France is organizing, together with the United Kingdom, a ministerial forum in Paris on development finance. The British proposal for an international financing facility will be high on the agenda, as will the work on international taxation undertaken at the request of the French President. We must be bold, confident always that we can count on the countries of the region to move forward together.

Mr. President, my country has confidence in your institution and urges you, as well as the countries in the region, to continue resolutely along the path to the reforms that are a sine qua non to improve the quality of life of the region's people.

ADDRESS BY MR. ISAAC ALFIE, GOVERNOR FOR URUGUAY

It is once again our honor and privilege to attend an Annual Meeting of our Bank, this time in the historic city of Lima, capital of the first viceroyship in South America, with all the cultural and historical import that this entails. I would like to thank the Peruvian authorities and the Bank's Management for their organization of this Annual Meeting, and to express our gratitude to this city and its residents for the warm welcome extended to us.

The conditions prevailing in the region and in Uruguay as a backdrop to this Annual Meeting are radically different from those of a year ago. Output is expanding, the terms of trade are improving, and capital flows toward the emerging countries have resumed.

The data on the Uruguayan economy are highly encouraging. GDP in the fourth quarter of 2003 was up almost 16 percent from a year ago. Employment rose by 5.5 percent, exports increased by 18 percent in value and 14 percent in volume, and there was significant diversification of the export markets. Inflation was contained and the exchange rate stabilized. In the first quarter of 2004, this recovery has continued. Employment is expanding at comparable rates, exports are growing by more than 30 percent, industrial output is increasing by roughly 25 percent, and both trade and agricultural activity are showing robust signs of growth.

Our policy is aimed at strengthening the business climate for the private sector, as we are convinced that this is the true generator of wealth and employment in the economy and, in the final analysis, the basis for most effectively combating poverty. We have cut public spending in real terms by almost a third over the last two years. The focus of our efforts in the past year has been to reduce hidden costs in the form of prohibitions, regulations, or simply bureaucracy, open up the economy, and increase investment. Competitiveness and, ultimately, the real income level of a society are critically dependent on these factors.

When we met last year in Milan, my country was at a critical juncture, seeking a mechanism whereby it could avert the risks of suspending payments in the short term. We understood that finding a solution to the public debt problem would clear doubt from the horizon and create the minimum conditions required for consolidating economic recovery. We had no doubts about the approach but were less certain about the magnitude of the results. Following the restructuring of our sovereign debt, the growth of the economy has been explosive, as has the rebound in investment, which expanded by over 80 percent in real terms in the last quarter of 2003.

The role of the international organizations in general, and of the IDB in particular, was crucial to the success achieved in overcoming the situation when the voluntary credit markets were not open to the region.

We would like to share some of the lessons learned:

We must take note of the significance of a weakened cash flow. We cannot allow ourselves the luxury of putting at risk this fundamental aspect of any serious and responsible economic policy. There can never be too many measures aimed at strengthening fiscal solvency, and there is never scant virtue in prudent macro-economic management.

Budget tightening is an unsurmountable obstacle, and no matter how much it may pain us, sooner or later reality will tell us where the limits are. It is the duty of those of us who manage society's resources not to boost financing requirements to a level that undermines the solvency of the public sector. In technical terms, we must constantly ensure that the debt transversality condition is met.

If we genuinely wish to be able to apply a countercyclical fiscal policy, we must maintain a sufficiently low debt-to-GDP ratio to have sufficient space to do so.

It is important to have a credit market in local currency. Uruguay took a fundamental step forward in October 2003 when it successfully floated a bond issue on the international market in its own currency. This issue was increased in early March.

Respect for preestablished rules as they are most widely accepted, as well as for contracts—despite all the effort this entails—ultimately pays off, and with interest.

Having a well-designed social safety net, which can be strengthened in a rational manner in periods of crisis, makes it possible to maintain social peace and adequately address the effects of crisis on the most vulnerable groups.

Trade openness is essential to development. I would like to emphasize yet again that the developed countries have a preponderant role to play in this regard, and that the best form of support would be to enable our output to be sold in those countries without artificial restrictions.

I would now like to turn to a few issues specific to the Bank.

In 2003, the Board of Executive Directors approved a new capital adequacy policy intended to protect the Bank from the potential risk that could be caused by various economic and financial situations. This policy makes it possible to approach the discussion of the new financing framework with greater tranquillity and with sufficient margin of flexibility to define the optimal distribution of resources and their maturities.

Within this framework, we believe it appropriate to emphasize our strong commitment to the financial solvency and liquidity that the Bank must have. It is an absolute priority to maintain the rating we now have, failing which the cost will be paid by the borrowing countries.

Accordingly, it is necessary to strengthen macroeconomic monitoring of member countries in order to prevent excesses.

We must bear in mind that when we are discussing investment projects, the microeconomic and macroeconomic frameworks in which the economy functions are perhaps more important than the tangible investment. Consequently, policy reform programs are of capital importance.

To this end, we ask that the Bank prepare the relevant simulation studies, reflecting various structures of operations, amortization periods, and disbursement methods, so that they may be used as a tool in examining the new financing framework.

While the Bank has made progress with the identification and approval of new lending instruments, we believe that it would now be advisable to work on defining general criteria on flexibility that provide the Bank and the member countries with the necessary capacity to adapt to the new reality emerging following the crisis.

We enthusiastically support the option of increasing and improving IDB Group support for the private sector throughout the region, as it is a driving force for development. An important step in this regard is the Board of Executive Directors' recent approval of the Private Sector Development Strategy, which offers an integrated approach for the IDB, the IIC, and the MIF. Along these lines, we wish to stress the need for focusing assistance to the private sector on initiatives that are compatible with country strategies and based upon concrete business plans.

To implement such plans, we concur that the proper structure is for the IDB Group to have a single interlocutor for the private sector. This would give the IDB Group greater visibility, greater presence, and financial room for maneuver. In the meantime, it is essential to attain the greatest possible internal coordination among the various private sector windows of the IDB Group, and that there be a linkage with the area of the Bank that works with the public sector.

In keeping with these remarks, we endorse the proposal to create a coordination position at the highest level.

The formal establishment of the Office of Development Effectiveness and the very close work with the Bank's operational departments are areas of progress that we applaud.

In this connection, we find that the Bank is examining in depth its processes for formulating and supervising operations in order to improve its services to borrowers. We look forward to this initiative and urge the Bank to give priority to those operational aspects that ensure greater returns in terms of their development impact.

Regarding the MIF, as we indicated at the Special Committee of Governors, we support the replenishment process and believe it should be implemented independently of any decisions relating to reorganization of the IDB Group's private sector activities.

We congratulate the IIC for the measures taken over the past year targeting improvements in its operational efficiency and effectiveness.

We believe that a key challenge to the institution is posed by the Declaration of Nuevo León having set an objective for the IDB Group the tripling of credit support for small- and medium-sized enterprises in the region through the utilization of financial intermediaries.

In addition, we reiterate the need for member countries to demonstrate their support for the institution by paying in the allocated capital contributions to which they have agreed.

Finally, we wish in particular to stress the approval of the initiative on nonreimbursable financing for expanding the Bank's participation in regional public goods. We understand that this initiative will make it possible to consolidate the Bank's regional leadership even as it contributes significantly to the development of our countries.

For all of the institution's successes in 2003, to which we have not been able to properly do justice in this brief address, we congratulate President Iglesias and the Management and staff of the Bank, and honor their dedication and professionalism.

Our meeting this year is overshadowed by terrorist attacks involving much bloodshed over the past weeks, and by the immense suffering of many people caused by these events. I would therefore like to express my deep sympathy with the people and families affected. The international community is called upon to counter these terrorist and criminal acts by even closer cooperation.

I wish to thank our host country very warmly for the invitation and professional management of this year's Annual Meeting. I am particularly happy to meet in Peru, a country possessing a very rich historic and cultural heritage, but also showing a dynamic development into modern times.

Thank you, President Iglesias, and your staff who ensures the perfect organization and implementation of our meeting.

We all hope that the improvement of the economic situation in Latin America and the Caribbean will be there to stay and will not be adversely affected by recent uncertainties in the global economy. The return to economic growth, a continuously low rate of inflation, and structural reforms gaining momentum in the countries of the region give cause for optimism. The countries have undertaken substantial efforts to consolidate their budgets and it is good to continue on this path. Further attention should now be given to reinforcing the rule of law and property rights.

The slight economic recovery should be used to push ahead with measures aimed at reducing poverty. The income disparities, high unemployment and the continuous lack of social security for broad parts of the population still constitute the major challenges.

I therefore do support the IDB in its efforts towards the reduction of poverty. Supporting pro-poor growth is the key challenge for a development bank. All efforts to promote the public as well as the private sector must be measured in terms of their orientation towards this task. The Millennium Development Goals constitute milestones here which must serve as an orientation also for IDB activities.

Let me mention just one central Millennium Development Goal: access to clean drinking water. This is becoming an ever more pressing problem also in the region, especially in the fast-growing urban agglom-erations. In the Millennium Declaration, the heads of state and government have committed themselves to improving access to clean drinking water: the number of people without access to clean drinking water and to sanitation is to be halved by 2015. I wish to encourage the Bank to develop innovative concepts for its activities in that field, going beyond mere financing and, for example, promoting public-private partnership.

Looking back to what has happened since the last meeting in Milan, several positive developments in the IDB come to mind.

I explicitly welcome the fact that the Bank has successfully concluded its work on the various sector strategies. We now have seven strategies which provide guidelines for the Bank's activities. These strategies must now be translated into concrete projects locally, and the Bank's practices and procedures must be aligned.

I take as an example environmental protection, which is of special interest for German development cooperation in Latin America. I do welcome that the IDB recognizes environmental protection to be a cross-sectoral issue: mainstreaming environmental protection into all fields of action is undoubtedly the most challenging and successful strategy of preserving and sustainably managing natural resources. I urge Management to provide sufficient resources and training for Bank staff to follow through on this issue.

I also very much welcome the development of environmental safeguards and the new policy to protect indigenous peoples. Ensuring these safeguards has been—and will be in the future—a prime contribution of the IDB to the Camisea project. It is now time to have these policies in writing as a matter of transparency and accountability.

Overall, the Bank is playing an increasing role with regard to the protection of regional public goods, and I welcome the new financing mechanisms in this regard. I do not want to conclude my remarks on this without mentioning the fight against HIV/AIDS. Also in this field, the countries of the region are just at the beginning.

Since the last Governors' Meeting, the Bank has taken a number of important steps on the path towards an even more effective promotion of the private sector. The IDB is about to place its various activities into an overarching strategic framework. I do support this step and want to encourage the Bank to finalize its reform by providing organizational structures that assure coherent and coordinated action of its various entities. Furthermore, I believe that the Bank should play an important role in assisting countries to develop a more conducive investment climate.

I am pleased to note that the IDB has intensified its efforts for improved development effectiveness. The putting into place of a central work unit and the medium-term action plan envisaged for summer 2004 are important steps in order to strengthen a result-based management. I wish to encourage the Bank to use the achievement of the Millennium Development Goals also as a yardstick for improved development effectiveness.

Let me conclude by saying a few words about two upcoming events where the IDB must, in my opinion, play a significant role.

From June 1–4, 2004 the International Conference on Renewable Energies will take place in Bonn. I wish to invite you all very cordially to this conference. Federal Chancellor Schröder had announced this conference at the World Summit on Sustainable Development in Johannesburg in 2002. The aim of the conference is to develop, together with representatives from governments and different interest groups, strategies for a wider utilization of renewable energies in both industrial and developing countries. Latin America has the natural potential for a greater use of renewable energies, and must prepare itself for the time when oil and gas have run out.

It gives me pleasure that President Iglesias will participate in the conference. I am confident that the IDB can play an eminent role in Latin America in enhancing an institutional framework for renewable energies and in developing the necessary infrastructure. Germany is very willing to assist such efforts.

Secondly, the EU-Latin America Summit will take place at the end of May in Mexico. Its principal theme will be social cohesion. Especially against the background that a noticeable reduction in poverty could not be achieved so far, this issue is of great immediate importance. Chancellor Schröder will take part in the meeting to underscore the importance that my country attaches to the cooperation between our two continents. The Summit may also offer an excellent opportunity for the IDB to demonstrate its competence in enhancing social cohesion in Latin America and the Caribbean to a broader public in Europe.

I wish to assure you, Mr. President, and your staff of my country's full support in your efforts to combat poverty and enhance social justice in Latin America and the Caribbean, together with the regional and nonregional members of the Inter-American Development Bank and the Inter-American Investment Corporation.

ADDRESS BY MR. RICHARD TEUTEN, TEMPORARY ALTERNATE GOVERNOR FOR THE UNITED KINGDOM

I should like to begin by joining the previous speakers in thanking the Government of Peru for hosting this year's Annual Meeting here in the historic city of Lima, and the Bank staff for their exemplary arrangements.

I would like to address three issues—the fundamental importance of the Millennium Development Goals, ways in which the IDB can improve the effectiveness of its contribution to achieving these, and the current debate on specific IDB instruments.

Last year's meeting in Milan was held at a momentous time—the war against Saddam Hussein had just begun. The recent atrocity in Madrid reminds us that the war against terrorism has not yet been won. The root cause of this insecurity lies in poverty and inequality in the world, leading to a more widespread awareness of global interdependence on issues such as migration, terrorism and the global environment.

This interdependence is one of the reasons the United Kingdom is committed to the achievement of the Millennium Development Goals aimed at halving the proportion of poor people in the world by 2015. We, therefore, very much welcomed the initiative of President Lula of Brazil and the IDB to hold a conference last November on Implementing the Millennium Development Goals. The resulting Brasilia Declaration points out that, "We are practically half-way between 1990 and 2015. This is the moment not only to evaluate the advances made so far but, more importantly, to intensify individual and collective efforts to fulfil the commitments in order to attain a future with peace, justice and welfare for the great majority of people, and better conditions for all." So, as the OAS Secretary General has said, 2005 will be a very important year, reminding us that there is only a decade to go until 2015. It will be a decisive year for us all, with the UN's conference being held to review progress towards the Millennium Development Goals.

In aggregate terms, Latin America and the Caribbean are not yet on track to reach all the Goals. The fact remains that over 130 million people—about a quarter of the population of the region—still live on less than \$2 per day; of these, nearly 60 million live on less than \$1 a day. As the ECLAC Executive Secretary has indicated, a step change is needed in the region's performance if it is to meet all its Development Goals.

You have pointed out, Mr. President, that Latin America is the most unequal region in the world. As the IDB's 1998 report *Economic and Social Progress in Latin America* said, development in Latin America is being held back by inequality. The low growth rates that affect this region are not only a cause of poverty but also a consequence of high levels of poverty. Sections of the population are being excluded from the benefits of social and economic development, from the political process and from access to justice because of their race, ethnicity or gender. Here in Peru, it is therefore appropriate to mention the IDB's commitment to producing a Strategy on Indigenous Development; the UK is pleased to be funding the consultation process for this. It will be as important that the Strategy delivers tangible benefits to the indigenous peoples of the region, as it is for the Bank to enhance the effectiveness of its efforts to tackle the exclusion faced by Afro-descendents.

Development finance—multilateral and bilateral—has an important part to play in reducing poverty and inequality, and the IDB is the largest source of development finance to Latin America and the Caribbean. With so many people in the region still to be lifted out of poverty, we must ensure that every dollar is used to maximum effect—whether through project aid, sector aid or budget support. For the Bank, as for all other partners in development, it is imperative to ensure that available resources are used to have a maximum impact, with a strong emphasis given to a results-oriented approach.

We very much welcome the creation of the new post of Chief Development Effectiveness Officer and the challenging agenda that the IDB has set itself in this regard. The time-bound action plan will be crucial in achieving this agenda, as will be the provision of adequate staffing and resources for the Development Effectiveness Unit and IDB support to build the capacity of borrowing members. A key prerequisite will also be close cooperation between the Unit and the Human Resources Department to ensure that staff face the right incentives to adopt this agenda throughout the Bank.

There are two other critical areas of development effectiveness in which the Bank should build on recent progress. The first is donor harmonization. We welcome the Bank's increasing commitment in this area—both at the multilateral level and in specific countries. I should especially highlight the Bank's strong leadership role in donor coordination in Honduras. This offers important lessons for the Bank's work elsewhere in Latin America and the Caribbean. I hope, too, that the Bank will participate in, and learn from, the forthcoming Joint Country Learning Assessment of donor alignment in Nicaragua that is taking place under the auspices of the OECD Development Assistance Committee.

The second area is lesson learning within the Bank. We recognize the Bank's wealth of operational experience but believe that much more could be done to systematize and disseminate lessons from this experience to create a true learning and knowledge culture. Such a culture would further enhance the quality of Bank assistance.

As we begin reviewing the Bank's lending framework, and the balance between investment and policy-based lending, the issue of development effectiveness becomes even more crucial. In principle, the UK is prepared to give serious consideration to increased use of Policy-Based Loans. However, in order to make a rational decision on the balance between these and investment lending, we need evidence of the impact of the Bank's existing portfolio of Policy-Based Loans and to make ex post evaluation and measurable performance indicators a standard feature of all such loans.

Finally, I should take this opportunity to reiterate my Minister's welcome for the proposal to push ahead with the replenishment of the Multilateral Investment Fund, given the valuable role it is playing in promoting growth that will reduce poverty. However, as he indicated, we are concerned that reemergence of the proposed PRI-IIC merger would hold up the replenishment and possible UK participation.

Mr. President, no institution is better placed than the IDB to advance understanding of the challenges and opportunities which globalization presents to Latin America and the Caribbean in terms of investment, trade and regional integration. The UK looks forward to strengthening its cooperation with the Bank in support of the objective for which we are all striving—a region free of poverty.

It is an honor for me to participate as a Governor in this Annual Meeting for the first time. The IDB is Colombia's main source of multilateral financing, and its countercyclical support has helped us overcome difficulties and revive growth in our country.

In August 2002, Colombia embarked on a process of political and institutional change thanks to the firm mandate that our people granted to President Álvaro Uribe. Today, 19 months later, we can state that the Colombian people have regained trust, security and hope in a country that was urgently clamoring for decisive action.

The first pillar of this process is the Democratic Security Policy. A firm decision to restore law and order to the nation, in the framework of respect for democratic institutions, is now showing results that need reinforcing. Let me mention a very elementary and basic example: vehicle flow on our highways increased by 30 percent in 2003. I know it is hard for many of you to understand the profound significance of this very simple piece of data, because fortunately you have not suffered the senseless scourge of violence perpetrated by groups that take up arms against legitimate institutions. Each family who reclaims Colombia's highways, each small roadside business that is set up, is one more example—saying more than any statistic could—that confidence is returning and, with it, a sense of ownership and empowerment, a sense of nationhood and citizenship. This is further supported by other equally simple but significant facts for a country that has been so buffeted by terrorism: for example, the number of families displaced by violence fell by 50 percent in relation to 2002.

The second basic pillar is the fight to restore macroeconomic stability through a strict program of fiscal adjustment and far-reaching reform of public administration at the national level. In areas as sensitive as the pension system and labor market policy, the government has not shrunk from implementing reforms carrying a high political cost, but which are sustainable in the long run. This commitment will be maintained.

The results are beginning to show through. The country is starting to shake off the lethargy of the last several years and has embarked upon a process of visible and widespread recovery. In 2003, GDP grew by 3.6 percent, the highest rate since 1995. More important than the figure itself is the fact that this growth was driven by fast-growing, private sector investment, which increased by 21 percent (11.64 percent of GDP), while our exports rose 9 percent in dollar terms.

We have not been alone in this process. The backing of the IDB has been fundamental. In 2003, the Bank approved the largest lending package that any multilateral organization has ever granted to Colombia. These funds made it possible to protect social spending during the adjustment period, support social security reform, invigorate the housing sector and make the hospital system more efficient.

But the Bank has not only been present through its lending instruments. Currently it is sponsoring the establishment of a consultative group that invites the international community to participate in creating sustainable programs to enable our campesinos to form part of the legal economy.

The Bank is also developing the first poverty reduction strategy in a middle-income country, aimed at charting a long-term State social policy that will transcend political and business cycles and make it possible to improve living standards among the most vulnerable population groups.

In 2004, we hope to see the first action plan for private sector development, in which the Bank Group windows that target this sector will significantly increase their exposure and identify innovative means to support the productive sectors, develop capital markets and promote a climate for investment.

In 2004–05, the Bank will support us with loans for improving the public utility regulatory framework, reforms to enhance our competitiveness in order to meet commitments arising from upcoming free trade agreements, and reforms aimed at substantially strengthening the effectiveness of the State in the fight against poverty.

Recent Bank decisions are very much in line with the demands of the times we are living through. The adoption of a modern capital adequacy model and the creation of new lending instruments are just two examples of the way the Bank has been adapting to the needs of its clients, without undermining the institution's financial soundness.

The capital adequacy model should be seen as the starting point for reforming, in the near future, the lending framework the Bank offers to countries. Ceilings that restrict lending amounts and disbursement periods should be lifted. These make the Bank less flexible and ignore the proven capacity of its Board of Executive Directors and Management to take decisions that are consistent both with client needs and with the capital strength safeguards that should guide all actions in any bank.

Colombia enthusiastically supports efforts being made to create new lending instruments, in which a good start has been made with performance-driven and export-support loans. In this important area of its work, and in view of the new realities, the Bank clearly has to consider taking decisions such as the adoption of mechanisms for lending to financially sound subnational entities without sovereign guarantees, lending in local currency, greater flexibility in counterpart funding requirements, and eligible expenses, among others.

It is also very important to move forward on other fronts. The Bank's invaluable support through the emergency facility during episodes of crisis has averted incalculable social costs. Nonetheless, its short repayment term, along with other aspects such as the single amortization date, have been difficult for countries like Colombia, where economic recovery gains and the financial terms and conditions of this vital lending facility may not always mesh completely. This suggests the need to continue searching for ways to improve this product.

The Bank must continue responding speedily to the demands of the Latin American private sector, by strengthening its support windows with innovative, flexible and rapid instruments. Effective backing to the private sector cannot be provided without rethinking the course of IDB Group institutions that extend funding to this sector. Operation preparation times and excessive bureaucratic procedures make the Bank less effective and prevent support from arriving at the right time. In this regard, Colombia supports lifting restrictions on the sectors that are eligible for financing from the Private Sector Department (PRI) and the Inter-American Investment Corporation (IIC), and asks them to persevere in their search for innovative avenues for local currency financing for our business community.

With this objective in mind, an overarching strategy that engages the PRI, the IIC and the MIF to increase their financing and technical assistance programs cannot be delayed. In addition, the MIF needs to be strengthened with a new capital replenishment; the demonstration effect and social impact of its operations are sufficient justification for this.

The IDB should continue to promote trade and cultural integration among our peoples. The regional public goods strategy, INDES strengthening, technical assistance for countries in preparation for the FTAA, and the creation of the Inter-American Foundation for Culture and Development are all aimed in this direction.

Fellow Governors, the challenge that unites us today is none other than that of supporting the Inter-American Development Bank at a time of change, backing its soundness and dynamism, and helping it to responsibly, creatively and effectively perform—as it has done for so long—its mission of responding to the needs of its clients.

The IDB is a sound organization that is fulfilling and must continue to fulfill, as it always has done, its vital role in our region. Having come through several difficult years, the Latin American people are optimistic about the period that is now beginning, and we are embarked upon the task of making the progress we see the length and breadth of the region—modest as it may be thus far—both sustainable and lasting. Improving results and, more importantly, making them sustainable is our key challenge.

In this we are well aware of the importance for the region of having a Bank that is financially sound, and a Bank that is even more nimble to help find solutions to the problems that are thrown in our path as part of the everyday fascinating complexity of this part of the world, which is so rich in opportunities for doing things well.

On behalf of Secretary Snow, I would like to thank Peru and Minister Kuczynski for hosting our meeting. President Bush places great value on our relations with Latin America and the Caribbean, and on the work of the IDB.

Increasing Economic Growth in Latin America and the Caribbean

I am pleased that since we gathered together one year ago, important progress has been made in reestablishing economic stability following the shocks and uncertainties of 2002. Improved macroeconomic policies have underpinned many of these improvements, thanks to the leadership of many in this room.

With progress towards stability, policymakers can rightly focus on increasing growth. While the region is recovering—real GDP growth in the region is estimated at 1.6 percent for 2003 and projected at 3.8 percent for 2004—we can agree that growth has been unacceptably low for the region given its potential.

Raising economic growth—specifically through productivity growth—is the lynchpin for improving living standards. The link between growth and poverty reduction is unmistakable. In this current window of opportunity, reforms to lock in solid macroeconomic policies are essential. Many countries in the region are making progress in enhancing debt management, improving monetary policy, implementing structural fiscal reforms to strengthen tax administration, institutionalizing spending discipline, and reducing rigidities in public budgets.

But macroeconomic stability, while necessary, is not sufficient for spurring growth. Addressing microeconomic impediments is an indispensable part of the growth agenda. This means strengthening financial sectors and expanding access to financing for the private sector, particularly small businesses; eliminating labor market distortions; investing in education and infrastructure; lowering trade barriers; improving investment climates, fighting corruption, and encouraging entrepreneurship; and harnessing the full development potential of remittances.

Let me say a few words about the role of the U.S. in this effort, and what the IDB can do to support the efforts of countries in the region interested in pursuing this agenda for growth.

U.S. Agenda for Increasing Economic Growth in Latin America and the Caribbean

In addition to a large bilateral development assistance program, the Bush administration is pursuing a variety of initiatives to lay the foundation for higher growth in the region.

For example, we are promoting an ambitious trade agenda in the Hemisphere. The U.S.-Chile free trade area agreement is complete, and an agreement with five Central American countries and the Dominican Republic has been negotiated. We have announced negotiations with Andean countries and with Panama. We will replicate the successful trade capacity-building initiative in our dialogue with the Andean countries. Our efforts toward a Free Trade Area of the Americas continue.

We are also working to facilitate access to a powerful source of funds for development: remittances from workers in the United States. Building on the groundbreaking work by the MIF, the U.S. has worked to promote increased competition and expand access to the financial system. The U.S.-Mexico Partnership for Prosperity helped halve the cost of remittances from the United States to Mexico since 1999 and bring more remittances into the formal financial sector. The United States is committed to working with Latin America and the Caribbean to achieve the Summit goal of halving the average cost of remittance transfers to the region by 2008.

In addition, we are honoring our Monterrey Consensus commitments by tying increased development assistance to performance through the Millennium Challenge Account (MCA). This fiscal year, several countries in Latin America and the Caribbean are candidates for MCA funds.

The Role of the IDB in Increasing Growth

We have been working positively and constructively with IDB Management to help implement our vision for improved effectiveness at the MDBs. This includes emphasis on economic growth and managing for results. We believe the IDB must give greater attention to managing for results, and expect that through the Office of Development Effectiveness the Bank will establish a comprehensive results measurement framework.

President Bush is an active proponent of grant financing for development, particularly for the poorest countries. Therefore, we continue to urge discussions about how the IDB can provide grants to the region, including through the Fund for Special Operations.

As donors, we are very interested in seeing results from the use of our money and intend to monitor this more closely than in the past. But we think borrowing countries, who provide capital but also pay interest on loans, should be even more interested. Therefore, we would like to see the IDB publicly disclose information on progress during project execution. Transparency of results can be a powerful vehicle for increasing effectiveness and accountability.

Effectiveness and accountability are also hampered by corruption. President Iglesias made a bold commitment to several governance initiatives last year in Milan. Since then, the Office of Institutional Integrity was created, an important step. The new Information Disclosure Policy puts the Bank ahead of other MDBs in some areas. The review of procurement is another area in need of change. We want to work with Management to implement new policies and procedures to achieve accountable, transparent and efficient IDB corporate and project procurement systems.

Development of a vibrant, entrepreneurial private sector is indispensable to economic growth and poverty reduction. To catalyze growth, one of the IDB's most effective tools is its relationship with public and private sector actors. The Bank's new Private Sector Development Strategy recognizes this, and seeks to maximize the IDB's impact on private sector development. We look forward to Management's Implementation Plan to realize the promise of this vision.

Consistent with the Private Sector Development Strategy, we believe consolidating the Bank's private sector activities into one operational unit will increase efficiency and leverage the strengths of the IDB Group. Therefore, we would support a merger of the Private Sector Department into the Inter-American Investment Corporation to form a new IIC. Of course, this merger must be done on a scale that is financially viable for the Bank and new IIC. It must also preserve the focus on small and medium enterprises and retain expertise in private sector finance for infrastructure and the broadening and deepening of capital markets. It will likely require a high-level person to coordinate and bring order to the Bank's private sector activities, both operational and policy, on a temporary basis.

This proposal is strengthened by the Memorandum of Understanding between the IIC and Multilateral Investment Fund to collaborate on finance for small and medium enterprises. The IIC and MIF are each ideally suited to establish this program. We wholeheartedly support this initiative. By combining the strengths of the MIF and IIC in a coordinated fashion, we also believe the Bank Group will be well positioned to help realize the 2007 goal of the Nuevo León Declaration of tripling credit to SMEs.

The MIF is also the primary IDB vehicle to provide grant financing to the private sector. In the MIF, grant financing funded projects with demonstration effects to show how changes in public sector policies and practices create private sector benefits. We are particularly interested in seeing MIF resources directed towards the poorest countries to reduce the time it takes to start a business. If we are serious about creating jobs, the average number of days to start a business in Latin America—which at 71 is the highest of any region in the world—must be reduced.

In conclusion, I think that important progress has been made in strengthening the region's economies over the past year. The ongoing challenge is to lay the foundation for sustained economic growth. The IDB is moving forward on important initiatives to improve the overall environment for growth. By working together, we can create and maintain the policy and institutional environment that underpins lasting development and makes assistance truly effective. The United States is committed to working closely with all the countries of the region in this effort.

Introduction

On behalf of the Belgian government, I would like to express our gratitude to our hosts, the Government of Peru and the people of Lima, for their warm hospitality and for hosting these Annual Meetings. Although this is not the first time I am attending an Annual Meeting, it is still a great pleasure and privilege for me to be present here, because it is a timely opportunity to reflect on progress made over the last year and the challenges facing the region and the institution.

Regional Developments

Last year the region's economic prospects looked rather bleak, after two years of stagnation or even recession. But now, the pace of economic activity in the region is increasing and the economic outlook for 2004 seems rather good, with GDP growth of about 3.5-4 percent; inflation seems to be under control and currencies have stabilized. Economic growth provides the best opportunity for the region to reinforce economic, fiscal, and structural reforms. Citizens and investors alike have to see that the governments of the region are addressing the problems in the area of efficiency of the public sector, the independence of the judiciary, and the fair distribution of their national income. Let us use this opportunity.

The region's current recovery, however, needs to be sustained, because the region's traditional disadvantages of overindebtedness, undercapitalization of private companies, low domestic saving rates, and excessive dependence on a few commodities or low value-added products do not disappear overnight. These challenges remain largely unchanged and the region must therefore continue to implement sustainable fiscal and monetary policies. As the region's main provider of external public resources, the Bank has an important role to play in addressing these challenges and assisting the region to instill a framework for sustained medium-term growth and improved equity.

Development Effectiveness and Management by Results

The Bank has an important role to play in achieving the Millennium Development Goals (MDGs). After Monterrey and Johannesburg, it has become important to demonstrate that the Bank is an effective and efficient instrument in providing multilateral development assistance to the region. The Bank is engaged in an intensive effort to make progress in managing by development results at the corporate level and we commend the Bank for the important steps taken in this direction since Milan. The groundwork has been laid on the financial front through the new capital adequacy framework and at the operational level through fine-tuning of existing lending instruments and the creation of new ones. However, we must admit that the Bank has made less progress than expected since March 2002 when Governors agreed on measures to enhance its development effectiveness.

Last year, the Governors confirmed that development effectiveness needed to be a priority for the Bank, and several of us pointed out that strengthening development effectiveness was important in order for the Bank to attain its foremost objective of poverty reduction. The Bank's priorities are known and all stakeholders have a common concern: they want to see the results of economic development and give national agencies and the Bank's staff the incentives to actually achieve results; stakeholders want governments and the IDB to become more accountable.

The problem is not one of agenda setting, but of speed and quality of implementation, and also of evaluation. What we need is to set benchmarks with built-in time schedules. The goals are known: they are the internationally agreed Millennium Development Goals.

The President of the Bank emphasized in his closing remarks of last year's Annual Meeting that development effectiveness needs to become pervasive and that it is not an issue that can be solely tackled from the perspective of Bank lending. We agree with this; the Bank can and should help national governments to improve their use of resources to implement economic and social programs in order to reduce poverty in the region.

The primary task for the Bank now is to accelerate the implementation process in order to ensure the Bank's accountability. The effort must continue and therefore we welcome the recent announcement that the medium-term action plan aimed at creating a comprehensive development effectiveness system in the Bank will be ready by mid-2004.

I also would like to reiterate that development effectiveness involves all multilateral development agencies and that coordination among multilateral development banks (MDBs) is therefore extremely important. In addition, Belgium wishes to emphasize that partnerships and coordination with other development agencies, including bilateral, should be part of the medium-term action plan. Borrowing member countries have to manage a multiplicity of individual donor projects and initiatives. Strategic alignment, harmonization, and coordination among all involved are therefore key challenges to avoid any overlapping of activities among institutions and to create synergies.

I have to admit that, looking at the enormous social and economic disparities in the region, I'm not fully convinced about genuine local ownership of structural reforms, achieving MDGs, or managing by development results. Appearances can be deceptive and I have the impression that there is a gap between rhetoric and reality. For sustainable poverty reduction to be achieved, political will and commitment are needed. It is up to the region to demonstrate that the problems are being addressed.

Private Sector Development

To foster economic growth, private sector development is crucial. In Latin America, small businesses are a particularly important source of economic growth and job creation. Supporting the private sector is therefore a priority for the Bank Group. We welcome the efforts made over the past year to revitalize the Bank's private sector activities and to improve the coordination between the various entities of the IDB Group involved in private sector finance.

We fully subscribe to the adoption of the Private Sector Development Strategy, which recognizes the central role of country programming in setting priorities. The financing of productive capacity building is central to any development strategy. Creating an enabling environment for investment and enterprise development is essential for building productive capacity and is obviously the most important strategic choice for the Bank. Equally important are the policies that developing member countries can introduce to encourage investment. Developing member countries can take steps to facilitate sustained investment flows. These steps include increasing the transparency of investment regimes, nondiscriminatory treatment of investors, development of rules on investment protection, and allowance of free capital transfers. We would also like to emphasize that it is important that private sector operations contribute to the Millennium Development Goals. The strategy's main thrust seems to be that economic growth is a necessary condition for reducing poverty; however, we all know that this is not a sufficient condition.

What we like in particular about the Private Sector Development Strategy is its modesty. It is now important to carefully sequence the steps required to implement the strategy and to fine-tune the strategy at a later stage. We would therefore like to ask the Bank to present as soon as possible an explicit and prioritized medium-term roadmap of actions. Once an agreement has been reached on the implementation plan, we can move forward with the strategy itself and consider enlarging the scope of private sector operations.

We must admit that there is a gap between our expectations and the progress made regarding a suitable structure for the Bank Group's private sector activities. As I indicated last year, Belgium supports a solution that would introduce a clear separation of private sector operational risk from the Bank's public sector activities.

We have followed with interest the developments in this area and will continue doing this, and are ready to consider proposals to further develop our private sector activities. I wish, however, to warn about overreaction: a healthy balance between private and public sector activities needs to be maintained. Both activities need to complement each other. I do hope that the Management of the Bank, including the high-level coordinator, will take this message into account. Time will also tell if this high-level management position will contribute significantly to the establishment of an efficient and effective framework of coordination between the IDB, IIC, and MIF.

In conclusion, I want to thank you, Mr. President, and also the Bank staff for your excellent work in trying to address the Bank's shortcomings and to understand the full scope of the corporate reforms needed in order to deliver results. Implementation and evaluation are vital.

I first want to thank the Government and people of Peru for their kind welcome and for the excellent arrangements made for our meeting.

Yesterday's speech by President Iglesias sends a message of hope. After several years of sluggish growth, the tide seems to be turning. This is certainly a welcome change since our region has been lagging behind other parts of the world with respect to the improvement of economic conditions for its citizens.

In his remarks, President Iglesias also talked about the achievements of the IDB during the past year. We are particularly pleased to see that a number of internal issues have been addressed, all of which will make the Bank a stronger voice for positive change. We wish to recognize in this regard the implementation of the capital adequacy framework and the establishment of the office of Private Sector Credit Risk Assessment; the approval of the Information Disclosure Policy; the growing status of the Office of Institutional Integrity; and the approval of Codes of Ethics for both Management and the Board. The creation of an independent Audit Committee remains a work in progress. Canada has encouraged and applauded these efforts; we will continue to be involved in their development. Recent events in the corporate world have certainly underscored the need for transparency and accountability.

However, as we look ahead, there are some other critical issues that the Bank must face. In my brief remarks today, I would like to focus on three of them: development effectiveness, the future lending framework of the Bank, and its role in private sector development.

On the issue of development effectiveness, you will recall that when we approved the 2002–04 lending framework we included a paragraph on measures that the Bank would adopt to "strengthen the development effectiveness of all the instruments of its lending categories." Now, two years later, when we will soon begin discussions on a new lending framework, we must conclude that while the Bank has made some progress in regard to development effectiveness, it has not moved as far or as quickly as many of us expected.

On the positive side, Management has recently announced the appointment of Mr. Lionel Nicol as the interim Chief Development Effectiveness Officer. We welcome his appointment and we can assure him that we will support him in his efforts. At the same time, we call on the Bank itself to ensure that his office has the support required to enable him to fulfill his mandate.

We also have before us—as one of the documents for this Annual Meeting of Governors—the Progress report on Management's actions in 2003 and future actions to enhance the Bank's development effectiveness. This document lists a number of actions that have been taken including: the preparation of new guidelines for country strategies, steps to enhance the quality at entry of projects, proposals to improve project monitoring and project completion reports, and the establishment of a Task Force on Retooling Bank Operations.

We applaud these initial steps since to us they are signs that the Bank is headed in the right direction. But greater effort must be expended by the Bank to follow up on their implementation. Now that a Chief Development Effectiveness Officer is in place, the Bank must move with greater commitment to make development effectiveness a priority. In an era in which there is great demand for development resources but limited funds, the Bank needs to be able to show to its shareholders that its activities—through all its lending instruments—are helping to improve the living conditions of the people in the Americas.

I would now like to turn to my second topic, the Bank's lending framework. During the latter half of 2001, the Board of Executive Directors and then the Committee of the Board of Governors spent considerable time discussing—indeed negotiating—a new lending framework for the Bank. This framework was eventually presented to Governors as the Agreement on Measures for Enhancing the Response Capacity of the IDB.

As we have seen during our Committee of Governors' meeting here, the question of the lending framework is once again on our agenda as the current agreement expires at the end of 2004. It seems to me that if we are to arrive at a consensus prior to the end of this year, then we need to repeat the process we followed in 2001. We would suggest that the Board of Executive Directors undertake some initial discussion on the topic, and then the Committee of the Board of Governors be convened once or perhaps twice in the second half of this year to finalize an agreement.

As a means of generating some initial thinking on the subject, I would like to posit three questions that we see as fundamental to those discussions.

The first question is what is the appropriate blend of emergency, fast-disbursing and investment lending for the IDB. In addressing this question we will of course need to bear in mind a number of factors. These would include: the development challenges facing the region and the expressed needs of borrowing member countries; the comparative advantage of the IDB with regard to other lenders in the region; the skills and knowledge of Bank staff, at both Headquarters and its 26 Country Offices; and the financial well-being of the Bank.

We would suggest that a second question that needs to be addressed regards what conditions should prevail within borrowing member countries for the Bank to move to more flexible, more rapidly disbursing instruments. For the past few years, much of the development debate has focused on the importance of country ownership and of ensuring that donors do not impose too heavy an administrative burden on borrowing countries. Canada agrees with these principles and we support, in general, the use of more flexible instruments when circumstances warrant. But we have not yet had sufficient discussion in this Bank on what those circumstances are. Nor, in our view, have we yet had sufficient discussion about how to assess the impact of such operations. If we want to make a case for greater use of such instruments we need to be able to show that they are better suited to conditions in borrowing member countries and that they are equally, if not more, effective than more traditional investment lending.

The third question that we need to address is what steps can be taken to improve the efficiency and effectiveness of all lending instruments of the Bank. In the past year, the Bank has experienced a decline in investment lending. This may be a temporary situation or it may be a harbinger of a longer-term trend. We do understand that in part this decline reflects a concern of borrowers about the procedures pertaining to such loans. As part of the process leading to discussions on the lending framework, the Bank should thus be examining its internal procedures and processes to help make investment loans more attractive to borrowing member countries.

Mr. Chairman, I hope that as our discussion on the lending framework proceeds over the latter part of this year, we will find ourselves in a position to deal openly and frankly with these and other important questions pertaining to lending operations. I also would hope that by the end of the year, we will have reached agreement on a new framework that will help place the Bank in a position to be able to continue to contribute effectively to the economic and social development of the region.

I would now like to turn to the role of the IDB in private sector development, first referring to the landmark report of the UN Commission on Private Sector and Development, co-chaired by Prime Minister Paul Martin and former President Ernesto Zedillo. To quote from that report:

> "The Commission believes that the primary responsibility for achieving growth and equitable development lies with developing countries. This responsibility includes creating the conditions that make it possible to secure the needed financial resources for investment. Those conditions—the state of governance, macroeconomic and microeconomic policies, public finances, the financial system and other basic elements of a country's economic environment—are largely determined by the actions of domestic policymakers. Their challenge is to
> * launch reforms that bring about further changes in institutional frameworks to unleash and foster the private sector."

In our view, it is precisely in this area of endeavor that the IDB is best placed to assist its borrowing members—by building the enabling environment and acting as a catalyst for new approaches. It can work with borrowing member governments on the difficult regulatory and business climate improvements necessary for the private sector to flourish. It can manage risk in ways private institutions cannot. It can promote public-private partnerships.

The Bank's private sector development efforts should, we believe, be firmly rooted in its country strategies, and be subject to the same development effectiveness disciplines as other kinds of programming.

Private sector development will drive economic growth in the region, it will provide incomes for the poor and—under the right conditions—will reduce inequality. There is clearly a role for the IDB, but it must be a judicious and well-considered one.

We look forward to participating in upcoming discussions of replenishment of the Multilateral Investment Fund. We are pleased with the results of the independent evaluation of the MIF, and we endorse the action plan for moving the replenishment exercise ahead. We will of course want to see clearly what role is foreseen for the MIF, and other elements of the Bank Group, with respect to SME support.

Canada appreciates the Bank's responsiveness to the Summit of the Americas Plan of Action, and we value highly the support the Bank has given to borrowing countries in their efforts to internalize and achieve the Millennium Development Goals. As we move closer to the mid-way point to the target date for the achievement of the MDGs, it may be appropriate for the Bank to assess how well it and its regional member countries are doing in this regard. This assessment might well provide a useful context for our work on the lending framework.

We realize the shortage of grant funds is restricting technical assistance and the financing of regional public goods. The blending of Ordinary Capital and soft resources could, if allowed, offer a remedy. Because of the fundamental importance of capacity building through technical assistance, we strongly urge the Bank to find ways to overcome this obstacle.

We would also encourage the Bank to make continued efforts in refining its approach, as it moves ahead in the crucial area of performance-based allocations—a key element in improving the development impact of our investments.

So the main concerns in our thinking about the Bank are, again, development effectiveness, the private sector, and the future direction of IDB lending. And in closing, I will just add a few words about Haiti.

All of us share a desire to see Haiti resolve its present difficulties and move toward security, democracy and a better life for all of its people. To this end, Canada has recently contributed nearly US$10 million for humanitarian assistance and support for UN agencies and the Special Mission of the OAS. We have sent some 500 soldiers for peacekeeping duties. And, through the programs of the Canadian International Development Agency, we will continue to assist Haiti's development efforts, with emphasis on such areas as basic education, health, economic development, human rights, justice, and security. We consider the involvement of CARICOM and the CDB also to be crucial.

We see progress in Haiti as a critical test for our region—just as we consider the Bank to be a critical development institution for our region. That's why we are eager to see this Bank live up to its full potential as agent of change, as instrument of economic and social advancement, and as a force for progress toward a better life and future for all the people of the Americas—with priority, always, for the poor.

It is a great honor for me to address this assembly today in my capacity as Minister for Economic Affairs and Finance and Governor of the IDB Group for Haiti. Allow me to echo my colleagues who have spoken before me in thanking the Government of Peru and the mayor and people of Lima for the warm welcome extended to the Haitian delegation and for the excellent organization of this Annual Meeting of the Boards of Governors of the Inter-American Development Bank and the Inter-American Investment Corporation. I would also like to express my appreciation to the Secretariat of the Bank, which has spared no effort to ensure the success of this meeting.

For me personally, it is a source of special pleasure to once again enjoy, after a number of years, the legendary hospitality of the Peruvian people.

As you have surely observed over the past months, Haiti has been a recurring headline in the international press. Inasmuch as the details are well known to all, what we need to keep in mind overall is that the Haitian people's decades-long pursuit of democracy and a better standard of living has unfortunately not borne any tangible fruits. Nearly half of Haiti's citizens live in extreme poverty, a situation that is compounded by insecurity in many and varied forms.

The problems of governance that ensued after the contested elections and a spiral of violence culminated in the departure of the previous government team.

The rest is history.

On the first of March, Haiti embarked on a new phase. As stipulated in the Constitution, the Chief Justice of the Supreme Court, Mr. Boniface Alexandre, was named acting President. A tripartite commission comprising a delegate from the party of the outgoing President, a delegate of the opposition, and a representative of the international community named, by consensus, a seven-member Council of Sages representing the various sectors of the country.

The Council considered the candidatures of a number of prominent Haitians and, after conducting interviews, recommended to the interim President that Mr. Gérard Latortue be appointed Prime Minister. Once the choice was confirmed, Mr. Latortue—in consultation with the various sectors—formed a transition government made up of independent public figures.

The mandate of the government, of which I am proud to be a part, is to hold democratic, honest elections within two years and, in the meantime, to lay the foundations for better governance. Emergency measures are under study that would help create jobs, lower the cost of living, foster social reconciliation, and reduce extreme poverty.

To underpin our action during this period we propose to establish a number of benchmarks and guidelines. It is our hope that these will serve both as guideposts and as beacons for future administrations.

I would like to take this opportunity to express my government's gratitude to the friendly countries who have stood unflaggingly by the side of the Haitian people in their struggle to improve socioeconomic and political conditions. Special mention should be made of the efforts of the Organization of American States and the Central American Common Market (CARICOM) to help us settle our differences through dialogue and consensus building.

We have also taken note of the Inter-American Development Bank's strong show of solidarity with the Haitian people. Under the leadership of its president and with the backing of the Board of Executive Directors, the Bank has kept its technical staff in the country and has accelerated its reengagement process.

As a result, the IDB is today in a position to resume its activity in Haiti promptly, as soon as officials in charge of the projects approved last year have been appointed or confirmed. On behalf of the government and personally, I would like to ask that Mr. Iglesias convey our sincere thanks to the Region 2 manager and specialists and to the staff of the Country Office in Haiti.

It would be a commonplace to label 2003 an especially difficult year for Haiti, with nominal growth of 0.4 percent after three consecutive years of unequivocally negative growth. Indeed, it has been quite some time since Haiti has had what could be termed an easy year in any sphere. The 2002–03 fiscal year began with the signing of a staff-monitored program (SMP) with the International Monetary Fund, which made it possible to set parameters for narrowing the budget deficit, phasing out ministerial current accounts, and defining a global plan for the clearance of arrears. At the end of the first four months of the 2003–04 fiscal year, however, the program suffered some major setbacks, and deficit financing through monetary measures reached alarming levels of more than 3 billion gourdes (approximately 3 percent of gross domestic product). Comparing this figure with the 4 billion gourdes recorded for the entire preceding fiscal year underscores the magnitude of the financial problems Haiti is facing.

All hope is not lost, however. At the Ministry for Economic Affairs and Finance, we are confident that we will be able to capitalize on the efforts made thus far. The government will soon resume its talks with the IMF on the terms of an arrangement for eventual renegotiation of a program under the Poverty Reduction and Growth Facility. It is to be hoped that other partners will quickly join us in our efforts to narrow the fiscal deficit and combat poverty.

In conjunction with the launching of an emergency plan, the key elements of the medium-range recovery plan that we would like to propose to our partners address several pressing challenges. First and foremost is what kind of growth will help to reduce poverty and inequality with a minimum of social conflict. In this regard, the new administration will take steps to:

(i) pursue a macroeconomic policy package consistent with short-term stability and long-term growth;

(ii) strengthen the role of the private sector as an engine of growth;

(iii) formulate and implement poverty reduction programs aimed at broadening the social safety net, enhancing the delivery of social services, especially education, health care, and the payment of reasonable social security benefits;

(iv) launch initiatives to make the production system generally more effective by improving physical infrastructure, strengthening public institutions and building human capital; and

(v) boost internal savings so as to finance a higher percentage of investments, while ensuring efficient use of capital.

I would like to take advantage of this occasion to say that the Haitian government appreciates the recent initiative of the World Bank to assemble donors for an initial exchange of views on the key economic problems facing our country in light of recent political events. We will soon be welcoming a mission of these donors on or around April 15. Working in cooperation with the respective Haitian institutions, the mission will be geared towards helping us to assess our short-, medium- and long-range needs in advance of the June pledging conference.

As indicated earlier, the staff-monitored program with the IMF and the settling of arrears with the IDB made it possible for the Bank to reengage with Haiti in July 2003 and rapidly resume activities. On December 31, 2003, disbursements stood at US$47 million, which was unfortunately not enough to reverse the net negative flow of resources. With the payment of US$2.5 million last week, the gap in funding flows widened even more, to Haiti's detriment.

We sincerely hope that the Bank will continue redoubling its efforts to expedite project implementation and increase disbursement flows, especially to the social sectors, and for rehabilitation of basic infrastructure. In this regard, the government will soon submit a package of specific proposals to the Bank aimed at speeding up project implementation and disbursements and reversing the negative flow of transfers.

The damage caused by political unrest these past few months has had fallout in all sectors. The government, the private sector, and civil society are working to assess the losses in money terms. The most conservative estimates are already in excess of US$600 million nationwide.

To cite just a few examples, school buildings and facilities—of which the country had too few to begin with—now need to be entirely rehabilitated or replaced. Many business establishments and thousands of microenterprises in the formal and informal sectors have virtually lost their operating base. The net effect has been a drastic drop-off in economic activity, burgeoning unemployment and dwindling tax receipts.

We must also tackle a number of serious and long-standing environmental issues in order to break the vicious circle that has led to Haiti being left with a choice between a “never-ending disaster” and a “disastrous end”.

Moreover, and perhaps above all, strong measures need to be taken within the framework of applicable legislation to ensure the safety and security of human lives and property.

To mitigate negative factors that could potentially lead to severe complications in an already difficult transition, the government is looking to undertake a vast program of job creation and labor-intensive works. We trust that all our partners—I repeat, all our partners, both Haitian and foreign—will find it in their hearts to work with us in this endeavor according to their capacities.

Haiti’s private sector has without a doubt been one of the hardest hit victims of the events of past months. It no longer plays its pivotal role in economic growth and job creation. Coincidentally, looking through the documentation distributed for our meeting here, I could not help but notice that one of the focuses of the IDB Group’s discussions has long been the adoption of a strategy for effective development of the private sector in the region.

Even though Haiti has thus far not been able to benefit at all from the expertise and assistance of the IDB’s Private Sector Department (PRI) or the Inter-American Investment Corporation (IIC), though it definitely has had support from the Multilateral Investment Fund (MIF), we welcome and commend the work undertaken to ensure more efficient coordination of these institutions and we support the idea of engaging a high-level coordinator to work on behalf of the president of the Bank to assure harmonization and effectiveness of the actions of PRI, the IIC and the MIF.

It goes without saying that the IDB Group should persevere in its efforts to actively identify investment opportunities in countries such as Haiti where such opportunities are less conspicuous, and to promote projects and encourage investors to take part in them.

Haiti has an extremely dynamic private sector that is eligible to borrow without sovereign guarantee and should be the object of such lending operations. We strongly support the granting of financial and technical assistance directly to private sector projects as well as effective involvement by this sector in national dialogue. The government also hopes to continue to receive from the IDB Group the necessary support for creating an enabling environment for private enterprise. In addition, this would help to reduce the country risk as well as project financing costs.

I would like to return for a moment to the work of the Multilateral Investment Fund, which got off to a very promising start in Haiti. However, problems associated largely with the political situation have kept our country from benefiting in recent years from the MIF’s full range of instruments, expertise and experience in order to strengthen institutions and undertake the necessary reforms for development of the private sector.

Despite the MIF’s active and very visible support for microenterprise in Haiti, I know that President Iglesias and the Manager of the MIF, Mr. Donald Terry, have always wished that the MIF could do more for us.

The Government of Haiti truly hopes that the MIF's work will not be slowed down or scaled back because of a scarcity of resources.

The government also hopes that Haiti will resume its place amidst the MIF donors. We furthermore support the proposed replenishment of resources of this institution which, as we all are aware, was created precisely in order to help solve the problems of countries such as Haiti. We feel it would be well for us to make a contribution to the capital increase, at the appropriate time, drawing on our own resources.

It is well known that the dual objectives of reducing poverty and fostering the private sector benefit from the promotion and development of microenterprise. We would therefore be happy to receive from the respective MIF departments the necessary instruments for taking part in this replenishment, in order to examine them as soon as possible.

Before closing, allow me to reiterate the commitment of the transition government—of which I have the honor of being a part—to work towards national reconciliation, better living conditions for the people of Haiti, the laying of a foundation for sound and transparent governance, and the holding of honest and democratic elections within a maximum of two years.

My last point is one that I wish to underscore especially: the government will be taking a very proactive stance in combating open or rampant corruption, both active and passive. Corruption has become an endemic ill across the region but has taken on extraordinary proportions in recent years in Haiti. To this end, we would like to set up—with the help of our friends in the international community—a unit within the Ministry of Economic Affairs and Finance tasked specifically with fighting corruption, to track down this malady wherever it may manifest itself in the government.

On behalf of Switzerland, I would like to extend my gratitude to the Peruvian authorities for their excellent and generous arrangements and their warm welcome in this beautiful country.

The Region

Ladies and gentlemen, I feel much more comfortable today than a year ago when looking back on the region's recent performance. After a long period of recession and stagnation that began in 1998, the region experienced economic growth in the order of 1.5 percent in 2003. Moreover, the immediate outlook is also promising, with economic growth poised to reach almost 4 percent in 2004. In other words, I am relieved to say that after one of its most severe crises in several decades, Latin America is set to return to the growth path from which it had been thrown off by the deterioration of international financial conditions and the slowdown in global economic growth.

Despite this cautious optimism, there is no reason to be complacent. The region's recovery is fragile and its mid-term prospects uncertain due to the legacy of the crisis of the past five years. Of particular concern is the deteriorating public debt situation in various countries, which will constrain the capacity of governments to support the economic recovery and risks increasing the region's vulnerability to external shocks. Moreover, most of the region's financial systems remain fragile, unequipped to accommodate sudden changes in inter-national financing flows, and not yet in a mood to finance new productive-capacity expansion.

Yet perhaps most worrisome is the fact that in many Latin American countries the public mood is one of frustration at the failure of the past decade of economic and democratic reform to deliver more tangible social and economic progress. Indeed, after some notable improvements, the incidence of poverty is once again on the rise, estimated to have increased by two percentage points to 44 percent since 2000, and unemployment has reached record levels. Moreover, the region remains the most inequitable region of the world, and social inequity is still rising in many countries. As a result of this sobering legacy, popular appetite to advance the free-market reform agenda has waned, and social and political unrest in some countries might even lead to a reversal of past reforms. In addition, although democracy has proven to be surprisingly resilient in the face of such adverse socioeconomic circumstances, the risk of unstable or even failed States in certain parts of the region can no longer be denied.

The Need for Continued Reform

I share the view that the disappointing return from the past decade of reform can be attributed to the following factors: (i) the region's chronic vulnerability to financial crises; (ii) the failure to fully implement macroeconomic and structural reforms; (iii) the lack of progress in implementing institutional reforms; and (iv) the region's entrenched inequality which has prevented economic growth from swiftly translating into poverty reduction.

I strongly believe that it would be a grave mistake to backtrack on the past reform path. Rather, the region should move ahead with its reform agenda, albeit adjusted in light of the recent experiences and lessons learned. The governments of the region are in the driver's seat for this process, and responsibility for success or failure rests ultimately with them. However, we are all committed to the achievement of the MDGs. In this regard, I would like to assure the governments of the region of Switzerland's full support, and I remain convinced that the IDB can strongly support this difficult process on the basis of its policy dialogue, analytical and sector work and lending operations. I would like to propose the following reform agenda.

First, governments must find ways to reduce the region's dependence on volatile external capital flows. The introduction of competitive exchange rates represents a first step in the right direction. Most importantly, however, is the need for financial market deepening. In an attempt to promote saving and borrowing in local currencies, governments of the region should vigorously pursue pension and financial market reforms. No less decisive are measures for strengthening the competitiveness of local producers in their own local markets by building up more adequate savings and credit institutions.

Second, although governments have demonstrated their commitment to fiscal discipline, they need to be more attentive to the need to restrain spending in good times so as to enlarge their room to maneuver to pursue countercyclical fiscal policies. Tax reform, in particular with respect to the mobilization of the resources required to strengthen institutions and to finance and implement urgent development programs, should be a priority in this context. Trade and regional integration are two important areas in which momentum has been lost during the past years. Enhancing the competitiveness of the economy, and an additional effort to develop the human resources for that purpose, is of utmost importance. It is also important that the region's policymakers renew their commitment to trade liberalization and actively seek a breakthrough in regional and global trade negotiations.

Third, governments must continue to pursue and deepen institutional reforms. Such reforms, arguably among the most diffuse and complex parts of the agenda, include measures and policies aimed at strengthening the rule of law, combating corruption and reducing the regulatory burden for businesses.

Fourth, governments need to step up their efforts in reducing their countries' flagrant inequality. There is a growing body of evidence showing that inequality has undermined the region's growth potential and that the creation of equal opportunities and a more equitable distribution of income are a necessary prerequisite for sustainable economic growth and development. In pursuing more equitable policies, governments should seek to introduce property taxes and progressive income tax regimes. In addition, it is crucial that governments undertake more to help the poor gain assets by facilitating access to education and vocational training, promoting land reform programs and introducing property titles.

Progress since Milan

I am very pleased to see that after much debate in the Board and a very constructive public consultation process the Bank has adopted a new Information Disclosure Policy. The new policy represents a quantum leap in terms of enhancing the Bank's transparency to the outside world and puts the IDB on the same level as the other MDBs. Of course, the new policy will have to prove itself during the upcoming year, its true value to be gauged by the extent to which stakeholders can make use of the information disclosed. Nevertheless, in my view the new policy clearly testifies to the Bank's ongoing commitment to strengthen its accountability.

Another major achievement of the Bank during the past year was the approval of the new capital adequacy framework which concluded the long and, at times, difficult discussions over this topic. I strongly welcome this approval since it equips the Bank with a capital adequacy policy that is equal if not superior to its peer institutions and should give it a sound financial footing to weather possible future financial storms. Moreover, as a further positive consequence of this new policy, the Bank will be able to set standard loan charges that are lower and more stable than under the previous policy and compared with other MDBs.

The introduction of the new capital adequacy framework has given rise to demands on the part of various shareholders to revise the new lending framework. Although it is somewhat premature to reopen this discussion, I am aware of the importance various shareholders attach to this topic and the topic of flexibility.

I believe that any revisions to the new lending framework must comply with demands for enhanced development effectiveness, not threaten the financial soundness of the Bank and must be in line with the Bank's mandate as a development institution, guaranteeing a fair share of resources to all borrowing countries. That said, I would like to express my concerns over the Bank's growing emergency lending portfolio. In my view the Bank should be involved less in helping to mitigate the consequences of financial crises, and much more in helping to prevent them. I would hence strongly welcome the reallocation of unused resources for emergency lending to other strategic purposes. In this regard, an option worth further exploring would be to deploy such resources for financial market reforms, trade and integration and private sector operations.

Last year, the Bank once again demonstrated its willingness to address the evolving needs of its borrowing member countries by adopting four new lending instruments. I welcome this momentum and would like to commend the Bank in particular for the development of the innovative and very promising performance-driven loan instrument. However, when viewing the list of new lending instruments scheduled for discussion this year, I wonder whether this long-standing effort has entered a phase of decreasing returns. Indeed, I believe that we have reached a point at which we should start exploring the idea of developing strategies for middle-income and low-income countries involving distinct lending instruments for each country group. I am convinced that such a differentiated approach would respond better to the changing needs of the borrowing countries than a further proliferation of instruments.

Development Effectiveness

I would like to express my regret that the recruitment of a new Chief Development Effectiveness Officer (CDEO) has run into unforeseen difficulties and that the scheduled work on enhancing the Bank's development effectiveness has hence been delayed. As repeatedly stated on various occasions, Switzerland attaches the greatest importance to this issue.

Nevertheless, I acknowledge the Bank's past and more recent efforts in this area. Among the steps initiated in 2003 to enhance the Bank's development effectiveness, I would like to single out for special praise the review of quality at entry, which will hopefully lead to the establishment of a QAG-like structure at the Bank, and the development and approval of the performance-driven loan instrument, which represents the first MDB loan instrument truly linked to results. Generally speaking, I believe that the Bank has made considerable progress in "doing the right things" (country programming) and in "doing these things rightly" (monitoring, measuring and evaluating).

The immediate challenge for the Bank is to develop a long-term vision and to make sure that all of the Bank's institutional aspects, including its culture and incentive framework, are aligned towards achieving results. Looking somewhat further down the road, the next major challenge for the Bank will be to enhance country ownership of the concept and to help the borrowing countries increase and align their capacities.

Addressing these challenges will be the responsibility of the newly appointed CDEO, to whom we wish to assure our full support. We are aware that implementation of this part of the agenda is particularly difficult and will require sufficient time. The first major step in this direction will be the elaboration of the medium-term action plan, which we look forward to discussing as soon as possible.

Private Sector Development Strategy

Mr. President, I would like to turn my attention now to a topic which Switzerland accords highest priority and which will remain at the top of the Bank's agenda this year: the Bank's role in private sector development. In this connection, I would like to thank the External Review Group (ERG) for its work and recommendations, which I have read with great interest. As it turns out, it is unrealistic to merge the Private Sector Department (PRI) with the IIC. I therefore welcome that the Bank instead focused on developing a coherent private sector development strategy which aims to increase the coordination, effectiveness and quality of the IDB Group's interventions in the private sector.

I support the new strategy and agree with its main thrust. In particular, the Country Private Sector Development Strategies promise to be an innovative mechanism to enhance the development impact of the IDB Group's private sector activities and improve internal coordination. However, I would like to emphasize the following expectations: first, it is crucial that the Bank coordinate closely with other institutions when helping to develop an enabling environment for business. Second, the IDB Group's private sector activities should focus on promoting SMEs and must achieve measurable results in terms of job creation and income generation for the poor and middle classes. Finally, the strategy needs to be followed up as soon as possible by a time-bound action plan, containing clear outcome indicators and specifying the institutional, human resources and financial implications.

Implementation of the Private Sector Development Strategy is a daunting task that goes well beyond overseeing and coordinating the IDB Group's activities. The person in charge of this task has to provide active leadership within the Group and impose a private sector mentality on operational departments. Moreover, this person must also develop a broader vision of the Bank's role in the private sector and explore various options, including the proposal to merge PRI with the IIC. Mr. President, although we welcome your proposal to appoint a temporary coordinator, we would urge that such a position not only have a coordinating function, but rather have full responsibility to develop and implement the IDB Group's private sector approach. While organizationally attached to the IDB, such a person would in practice manage all three private sector entities of the IDB Group. Such a set-up has worked well at the World Bank Group.

IIC

Following the losses of last year, I am very satisfied to see that the IIC is back on the track of financial profitability, achieving a small net income of US$2 million this year. Although this positive result reflects in part the improved economic situation of the region, it can also be attributed to the measures initiated last year. Indeed, the Corporation has recovered mainly by slashing costs. Hence, the challenge for the immediate future is to enhance its business operations. IIC Management has already taken steps in this direction by proposing promising follow-up actions stemming from the ERG's recommendations. Looking ahead, the major challenge for the IIC will be to find its role within the IDB Group.

Conclusions

In certain respects, the region and the Bank are in a similar situation: after difficult and challenging times, both are facing a window of opportunity for far-reaching reform. Whereas in the case of the region this involves reinvigorating its past reform agenda, the Bank should vigorously take on the challenge of implementing the proposed reforms in the areas of development effectiveness and private sector development. Flexibility and pragmatism, coupled with a sense of urgency, should be the guiding principles for both.

ADDRESS BY MR. DIEGO LUIS CASTELLANOS, TEMPORARY ALTERNATE GOVERNOR FOR VENEZUELA

Here in our region, we are witnesses to what are apparently paradoxical situations. Economies whose macroeconomic indicators appear to reflect a high degree of efficiency, redistributive market mechanisms based on increasing wealth, employment, and returns on such factors as technology, and a form of resource allocation that bolsters fundamental elements for the enhancement of well-being—such as supply and demand—contrast with progressive social discontent that threatens our democratic institutions. We believe that we are overlooking something in this paradox. We are witnessing a parallel increase in the type of exclusion that serves as a breeding ground for imbalances and poverty. This prompts us to ask ourselves: what part are our institutions playing in all this? Are they, perhaps, geared to complex, complicated accounting mechanisms designed for use in statistical yearbooks and for satisfying the egos of economic policymakers, or to simple policy mechanisms that permit the realization of the moral, spiritual, and material aspirations of our citizens? We ask ourselves: Are we cultivating our societies on a basis of inclusion or of exclusion?

The market economy provides us with a channel for the expression of our preferences, desires, and feelings. It is a pillar of democracy. But the crucial condition in this respect is that we must all have access to it. This is the challenge of development, of our institution: to bring about institutional change that will ensure that infrastructure, policy, and reforms are inclusive, that society is involved in forging its members' own destinies, that those who govern are aware of their institutional bounds and of the commitment they owe to society.

We need effective tools for development, tools that can be used efficiently in the creation of well-being and equity, tools that contribute to transparency and accountability for what is done and what goals are achieved. We cannot have a type of growth that is reflected solely in economic indicators and that has nothing to do with our happiness as a society. This is the central paradox that we must confront, and this is the challenge to be overcome by our institution in the next 20 years.

In Venezuela, we are committed to achieving growth on the basis of the increasing satisfaction of the aspirations of humankind. Education, health, housing, and drinking water are priorities for us, but so is the creation of a productive society in which people feel that they control their own destinies, where exclusion is uprooted, where growth reflects the workings of markets that are free from the types of asymmetries that generate positive indicators in tandem with striking inequalities.

To attain these objectives, we have employed mechanisms that are largely misunderstood; our missions, citing our teacher Simón Rodríguez, and our "delirium" embody a profoundly revolutionary philosophy: either we invent, or we fail. This places us apart and may subject us to criticism, but we are convinced that the results will serve as a showcase for the path to be taken by our region. A heterodox path that leads us beyond simple, elementary diatribe, beyond the question as to whether we are neoliberal or not, or whether we should abide by requisite accounting procedures.

We have undertaken literacy missions, missions to educate people in arts and crafts and to provide higher education, healthcare missions—such as the Barrio Adentro plan, which has provided healthcare on a mass scale to our poorest communities—and missions to give citizens a role in the production apparatus. We are now in a position where we will soon be able to declare Venezuela free of illiteracy. We have set ourselves the task of achieving, in large measure, the Millennium Development Goals, not in 15 years, but in seven. This is a policy commitment.

Democratic participation, whereby citizens are aware and avail themselves of their rights, has become a fundamental value. This is why Venezuela is in the news; we Venezuelans are engaged in a search for our own society and identity. Political education is the key to having active citizens and is our staunchest ally in combating social exclusion.

Venezuela wishes to attest to its commitment to continue to uphold the inter-American spirit and democratic values through the work of the Inter-American Development Bank and its institutions.

I would like to thank the Peruvian government and, in particular, our hosts in Lima for their warm welcome and hospitality at this meeting. In this session, we would like to share with you the most salient aspects of the Republic of Panama's economic and social development policy.

The year 2003 saw an upturn in Panama's economy. Gross domestic product (GDP) rose at a real rate of 4.1 percent, reversing a business cycle marked by deceleration and adjustment. Most sectors performed well, laying the foundation for the country to enter the global market.

Panama has focused on social reform, government finance, productivity enhancement, and support for strategic sectors, with an eye to creating the conditions needed to achieve higher rates of economic growth and sustained human development.

To that end, in 2000–02 the national government accorded priority to consolidating macroeconomic stability as a State policy. It therefore passed the Fiscal Responsibility Act—the product of national consensus on the urgent need to regulate public sector borrowing—with a target of reducing net government debt to 50 percent of GDP and net foreign debt to 35 percent of GDP, in 15 years. In addition to capping the fiscal deficit at no more than 2 percent of GDP, the act stipulates that when growth exceeds 1.5 percent, the increase in debt may not exceed 80 percent of the percentage increase in GDP.

This legislation also changed the State's budget apparatus. During the first year the law was in effect, it generated a primary surplus and reduced the debt-to-GDP ratios I mentioned earlier. For example, the ratio of total net public debt to GDP fell by 1.7 percent; projected over time, this will enable us to meet the target in half the time allotted.

To underpin these adjustments, a tax reform was approved with a view to boosting government revenue, improving the State's capacity to meet social needs, and making the tax system more equitable, efficient, and streamlined. Figures from 2003 reflect the progress made to that end. Tax collections rose nearly 10 percent over 2002. There was also a shift in the distribution of taxes, which has resulted in better income distribution while balancing the fiscal burden and incorporating economic agents that were paying little or no taxes.

In 2003, several components shaped the implementation of the government's economic policy. A countercyclical policy was adopted to consolidate the economic recovery; public debt management was made more efficient, which is essential for maintaining the confidence of investors and credit rating agencies alike; and state financing was kept at reasonable costs. I should also highlight the initiatives aimed at modernizing the State, such as implementation of e-government, the financial management system, and the foreign trade system, which use information technology to connect the State with the populace through more efficient and transparent management; as well as the initiative to restructure formerly State-run enterprises and activities.

These changes include an aggressive liberalization policy. In 2003, free trade agreements were approved and implemented with El Salvador and Taiwan, as well as agreements with the Dominican Republic and Colombia. Negotiations with Central America continued, Panama began talks with Singapore, and work was launched on an agenda for a free trade agreement with the United States. This is an important step in transforming and modernizing Panama's economy in the medium term. It will have a positive impact in the short term thanks to the perception fostered by a liberalization policy, which encourages direct investment.

To prepare ourselves and to address the new situation, we have worked to boost productivity in the primary and secondary sectors, enhancing the country's competitiveness. A law was passed to encourage domestic and foreign industrial and agroindustrial investment, in keeping with World Trade Organization standards.

In addition, steps were taken to promote competitiveness by creating conglomerates in areas such as agroindustry, technology, tourism, logistics, and transport.

In the context of the social policy—one of the main elements of the development strategy in 2003—the national government raised the minimum wage by 4.1 percent; together with the 13 percent increase in 2001, this helped to boost the purchasing power of lower-income workers by approximately 9 percent, outpacing average inflation over the last decade of 1.1 percent. Priority was given to meeting the needs of the disadvantaged population by improving its productive capacity through programs for sustainable development in remote areas, sustainable farm production, microenterprise development, vocational training for youth, and rural road construction, among others. These are all key elements in promoting job-creating activities.

These social and economic achievements were made possible by the work and commitment of President Mireya Moscoso's administration. We must acknowledge, however, that Panama still faces some major challenges. We must strengthen these policies to consistently achieve growth rates over 5 percent and to have the capacity to maintain macroeconomic stability during slowdowns in the global economy, so as to prevent an adverse social impact on our countrymen.

We are working to form a conglomerate in the Panama Canal for activities related to air, maritime, rail, and land transport and logistical activities, to further enhance our long-standing calling as a hub for trade and to help the Panamanian economy grow sustainably.

Moreover, although we have closed our fiscal accounts with low deficits in recent years, there are still limitations in terms of State financing. Panama will not abandon its efforts to increase social and infrastructure investment financed with domestic savings. To that end, it must rationalize public spending and craft a policy to reduce the size of the State—a policy that should be implemented during periods of growth, when countercyclical policies are not needed.

With this in mind, we find very fitting the Inter-American Development Bank's efforts to design strategies that help the private sector in our countries to become the true engine of development for our peoples. Nonetheless, we must not forget that our institution, through the Multilateral Investment Fund and the Inter-American Investment Corporation, has taken steps that have contributed to our progress.

At the end of the road, we want to see the necessary care taken to protect the original raison d'être of these institutions: development of our peoples, reduction of poverty, and inclusion of disadvantaged sectors.

As Latin America begins a new business cycle and, in the case of my country, as we approach a change in administration, we in Panama are aware that economic growth in the immediate future will no longer be determined by a recessionary cycle and that now is the time to promote structural adjustments that stabilize economic development and allow for equitable distribution of the fruits of that process.

In closing, I would like to present my compliments to the Governors, the Board of Executive Directors of the Bank, President Enrique Iglesias and the two Vice Presidents of the Bank, senior management, and the entire staff who work day in and day out so that our Bank can continue to promote progress in our countries.

I have the honor of speaking on behalf of Paraguay on the occasion of the Forty-fifth Annual Meeting of the Inter-American Development Bank and Nineteenth Annual Meeting of the Inter-American Investment Corporation. I add my congratulations and thanks to the Government of the Republic of Peru for its generous hospitality and excellent organization of this event in the beautiful city of Lima.

After seven years of recession, in 2003 the Paraguayan economy rebounded, with economic growth of 2.6 percent, closed the year with inflation at 9.6 percent compared to 14 percent in the previous year, and increased its international reserves by 50 percent. The fiscal deficit was brought down to 0.6 percent of GDP, which is significantly lower than the 3 percent it hovered at in the last five years and, above all, we were able to avert the imminent threat of a year-end suspension of payments. This effort culminated in the signature of a Standby Arrangement with the IMF, the first in 46 years.

In 2004, the economic recovery will continue, with prospects for growth of close to 3 percent, 8.5 percent inflation, and a primary surplus of 1.5 percent of GDP. These fiscal results are chiefly supported on the income side by a major tax administration effort and on the expenditure side by reform of the public sector pension system, which has been the largest component in the growing fiscal deficit in recent years. However, this economic recovery will not allow for sufficient growth in jobs to ease the country's 16 percent unemployment rate.

Our country's achievements and its prospects for this year are the result of the regional economic recovery, the 'boom' referred to by President Enrique Iglesias at the Monterrey Summit, and of the determined efforts of the current administration, which took office on August 15, 2003.

First of all, the government is resolved to restore confidence and credibility in State institutions so that public policies will be effective. The fight against corruption and tax evasion has begun to produce results, with an increase in tax revenues of about 40 percent. Also, with IDB support, the government has established a Government Procurement Bureau and launched an electronic portal for tender calls and purchasing of 203 agencies that make up the Paraguayan State. Also, the Ministry of Finance has established a Unit for Transparency and Participation to enlist civil society organizations in the fight against corruption.

Second, the government is committed to advocating governance and legal certainty so as to promote public and private investments. Last year, the new administration and the Congress agreed on a legislative agenda for six crucial bills to enable fiscal sustainability and stronger finances. So far, three have been enacted: reform of the public sector pension system, deposit insurance, and restructuring the internal debt. One house has cleared another bill—the Customs Code—and two others—the bill on administrative reorganization and fiscal adjustment and the bill on reform of the public banks—are being examined by Congress. These laws will allow us to build a fiscal and financial framework conducive to sustained economic growth. Also, this year the government and political parties have reached a consensus on the appointment of six of the nine Supreme Court justices, to begin the awaited judicial reform. We are working to build the institutions needed to enable investment and job creation, with a view to reversing 21 years of stagnation.

Third, the current administration is determined to improve the efficiency, effectiveness and equity of public policies. It has launched several initiatives whose results will be seen in the coming years. They include the creation of the Project Monitoring and Evaluation Unit, with external financing; the Business Environment Unit to remove obstacles and create incentives for private investment; and the Social Cabinet, with participation by the Ministry of Finance, to coordinate social policies, measure the efficiency and impact of social spending, and make headway in implementing the strategy for the reduction of poverty and inequity, in pursuit of the United Nations' Millennium Development Goals.

On behalf of my country's government, I would like to express my support and encouragement to the Bank's Board of Executive Directors and Management in their determined approach to development effectiveness. As a borrowing member country, we very much wish to ensure that our interventions—through investment or policy loans—have the desired development impact, particularly when operations of this kind impose obligations on future generations.

We also add our vote in favor of the replenishment of resources of the Multilateral Investment Fund. In its 10 years of existence, the MIF has had a significant positive impact on the region's private sector, and Paraguay is no exception.

We applaud the strengthening of Bank action with the private sector. We see approval of the private sector strategy as the first step in this direction and urge the Board of Executive Directors and Management to work carefully on its implementation. We hope that in the "country focus" the strategy will duly consider the diversity of the borrowing member countries and provide effective support for the smaller economies. In our view it is crucial in this process to promptly appoint a coordinator, in line with the report presented by the Board.

We support the initiative to improve the business climate. Paraguay was one of the first signatories of the Bank's Aide Memoire that served as a starting point for the work with the Bank. Our country is very interested in improving relations between the State and the market to generate genuine, sustainable employment that will contribute to the well-being of every member of society, as the ultimate goal of public policies.

We congratulate the Bank and its President for overseeing the recovery of our economies with professional integrity and without losing sight of the social responsiveness that has always been characteristic of the Inter-American Development Bank.

First of all, I would like to thank the Peruvian authorities and the city of Lima for their warm welcome and hospitality. It is a great honor to spend these days in such a beautiful country. I even had the pleasure to realize that we share the same colors—red-white-red—in our national flags.

Region: Economic Growth Prospects – Remaining Problems – Role of the IDB

The short-term economic outlook is quite favorable. Growth has resumed or gained momentum in most countries of the region. The last year already showed a rather positive trend. Growth expectations for the region for this year are on average up to 4 percent. Economic development has benefited from improved international conditions, like stronger demand from major industrialized countries. Also, financial market conditions have improved with capital coming back, albeit slowly.

Nevertheless, the medium-term outlook is still hampered by some uncertainty. Structural social and economic problems have not yet been resolved. Many of the poorer and more vulnerable social groups are still suffering. Poverty is high and social exclusion still a problem. There is a lack of employment possibilities, and wage inequality has not improved. This is the reason why, to a large extent, market reforms installed in the last years have been discredited. Confidence in the outcome of reform processes has weakened considerably.

Not only is economic management questioned in this context, but also the political system in general. We cannot be complacent about the extent of reforms achieved so far because there is a danger here: when people are disappointed with the results of democracy, this can evolve into a worrisome threat to democracy in its entirety. Therefore, it is still important to establish the conditions necessary for a stable political and eco-nomic environment.

A lot of work needs to be done in order to help the region meet these challenges. The Bank's task here is to provide the necessary support in analyzing and helping with crisis situations. Nevertheless, we want to emphasize that the Bank's core mandate must remain to act as a long-term oriented development bank focused on sustainable economic and social development.

Lending – Capital Adequacy Model and Policy

In 2003, the Bank committed US$7 billion, which signifies an almost 50 percent increase over the poor 2002 figure. Nevertheless, if one excludes the very sizable emergency loans, it becomes obvious that the declining trend in lending activities has not been reversed and is indeed quite worrisome. Investment projects—which aim at long-term, specific development objectives—only accounted for 23 percent of total approvals in 2003, while the fast-disbursing, policy-based loans surpassed investment lending with a quota of 25 percent.

As we all know, the lending framework adopted in early 2002 put a cap on the overall amount available for policy-based lending. Although we fully agree that fast-disbursing loans have an important role to fulfill, we would like to see that when the new lending framework is elaborated, investment lending will be shielded from the trend towards fast-disbursing instruments.

We appreciate that the Bank's new capital adequacy model and policy were finally approved last year. With the new policy, the Bank is well prepared to meet the requirements of rating agencies and international financial market actors. Moreover, the new policy and model allow more stable and lower loan charges for borrowers. With this, one important step was set: to allow the Bank to act predictably and countercyclically.

Private Sector: MDGs – General Framework – Coordination

Strengthening private sector activities in the region is still one of the main issues on the agenda. We recognize that the private sector must be supported to improve the contribution it can make to economic development. But economic growth alone is not enough. Growth is needed in which the poor are able to participate. Otherwise the Millennium Development Goals, especially eradication of extreme poverty, will hardly be achieved.

In general, transparent, stable and predictable conditions are necessary for encouraging private sector activities. Efforts to improve the overall business climate in the region should therefore be the prime strategic objective of the Bank. In this regard, the work to put political and structural changes on track to create a benign business climate must be continued.

We warmly welcome the new comprehensive Private Sector Development Strategy and the business climate initiative as a general framework to provide a roadmap for the IDB Group as a whole. This framework stresses the key function that the country level will play in the implementation of the strategy, an approach we fully support.

This framework should also help to guide essential organizational changes to ensure an effective structure for the implementation of the defined objectives. We would welcome an accelerated effort in establishing an effective coordination mechanism for the private sector arms of the IDB Group. As regards the creation of a coordination position, we can support the installation of a high-level coordinator on an interim basis directly reporting to the President. We also recall that this position needs clearly defined terms of reference and that the appointment should be made in a transparent process.

Direct support to businesses and projects should only go so far as additionality is ensured. In this regard, we would also recommend the Bank to act prudently in deciding in which economic sectors to expand. Moreover, as the financial resources of the IDB are not unlimited, the establishment of new activities must not touch the financial integrity of the Bank.

Although we support the private sector activities, we want to emphasize again that the IDB's core mandate must remain to act as a long-term oriented development bank.

Development Effectiveness – Culture of Results – Leading Role of the IDB

We fully support the Bank's initiative to establish a comprehensive development effectiveness system thereby creating a "culture of results". In this context, we welcome the creation of the new development effectiveness office with its recently appointed Chief Development Effectiveness Officer.

We are looking forward to the Bank carrying out an analysis of its instruments and processes from the perspective of development effectiveness. This should lead to the necessary definition of the long-term objectives of a Bank-wide development effectiveness system. An action plan describing the steps needed to move forward will be the logical result.

As it is important to use existing resources effectively, strengthening collaboration with other development agencies in order to exchange views and lessons learned is essential. Moreover, as a result of coordination and collaboration, all countries in Latin America and the Caribbean should be able to share in best practices. This should also help to avoid additional burdens on the countries' administrative capacities.

Moreover, we urge the IDB to establish a leading role in development effectiveness in the region.

Final Statement

Finally, let me take this opportunity to thank you, President Iglesias, and the staff of the IDB Group, as well as our Executive Directors and their staff for the professional work done during the last year.

After having asked the Bank to move things forward in several fields of activities, I would like to conclude by wishing the Bank and all its partners in development cooperation that we can summon up enough enthusiasm and energy to achieve the necessary results and the overarching goal of our efforts—which is, of course, poverty reduction.

ADDRESS BY MR. GERARD STEEGHS, TEMPORARY ALTERNATE GOVERNOR FOR THE NETHERLANDS

Let me begin by complimenting our Peruvian hosts for a most graceful and accomplished organization of this year's Annual Meeting of the IDB and IIC. Not even here for a week, I already feel at home, only feeling sad with the realization I will have to leave again in a couple of days. It has been said by some that Peru was special to the gods, who chose this part of the world to land from outer space. I do not necessarily share that belief in any great detail, nor have I come from that far—but I do feel that it would have been the right choice for them as it is for this Annual Meeting.

I will focus on the importance of private sector development for economic growth and poverty alleviation and the three prerequisites for effective and sustainable operations of the entire IDB Group, i.e., cooperation, development effectiveness, and financial soundness.

But before discussing the private sector activities of the Bank, I would like to share with you our perspective on a challenge that affects both regional and nonregional shareholders of this Bank. A challenge that, if addressed correctly, would be the centerpiece of a better business climate and result in productive jobs, profitable businesses, and poverty alleviation. And instead of costing money it will lead to higher tax returns. This truly sounds like a "free lunch" and many economists claim that "free lunches" do not exist. Well, perhaps they do exist.* The challenge I am referring to is reducing the cost of doing business.

Already within Latin America and the Caribbean one could observe conspicuous differences in national regulation. For instance, in the beautiful city of Lima the cost of starting a business is limited to less than a quarter of annual per capita income. However, it ranges from one to more than 300 percent in other capitals. And while fulfilling the required procedures can take over 200 days in some countries, the same firm would be set up within a week in Puerto Rico. This is specifically a challenge for the region, for which the Bank could certainly offer its support.

In a recent publication on doing business in 2004, the World Bank determined that heavier regulation is generally associated with greater inefficiency in public institutions, more unemployment, corruption, and lower productivity. Perhaps more importantly, excessive regulation was seen to have a perverse effect on the very people it was meant to protect. Given the dominance of microenterprises in the region, and the fact that reducing the cost of doing business will promote their growth and formalization in the economy, the benefits that can be reaped are obvious: not only higher economic growth, but growth that benefits particularly the more vulnerable population groups.

The Dutch economy would definitely also benefit from lowering the cost of doing business. Therefore, reduction of administrative burdens has been made one of our top priorities. This has led to a commitment to cut the burden by a quarter within this Cabinet period. During the Dutch Presidency of the EU in the second half of 2004, we hope to contribute to a strengthened European approach to the administrative burden.

The Dutch method is based on measuring the administrative costs related to regulations by putting a price tag on the information requirements, consisting of time and money spent to fulfill these requirements. They are multiplied by the number of times companies have to fulfill these requirements per year. This indicator helps to identify which parts of legislation need to be cut back, modernized, or harmonized without harming the intended policy objectives. For the Netherlands, this exercise uncovered a total administrative burden equivalent to US$21 billion of which approximately 90 percent is imposed on small and medium-sized enterprises.

I think this approach could be relevant for the IDB and its shareholders as well. Substantial progress in this region has already been made in completing first-generation reforms. Nevertheless, my example indicates that there remains ample opportunity to increase growth and alleviate poverty through deregulation.

We are convinced that the IDB Group can play an essential role in accumulating and sharing knowledge, assisting in regulatory reforms through lending and technical assistance, and regaining the necessary public support for policy reforms. In those countries that have PRSPs, the IDB's private sector strategies should clearly be linked to this process. We appreciate the efforts that resulted in the recently approved Private Sector Development Strategy. Since intensified coordination within the IDB Group is a prerequisite for a satisfactory implementation, we welcome the creation of a temporary high-level management position to guide this process.

With regard to expanding the mandate of PRI, I would like to emphasize the significance of expertise. The IDB Group should retain knowledge it has acquired in the fields of development effectiveness and credit risk mitigation, and build this type of expertise in new areas of operation. Expanding the private sector operations of the Bank into new sectors could increase its performance in the field of poverty alleviation. It would also diversify the portfolio.

However, given limited IDB resources and the minimum scale of activities required to build and retain sufficient expertise in a certain sector, we feel the IDB Group should avoid spreading itself too thin. A fine balance between expansion on the one hand and selectivity of sectors and due attention to the accumulation of more generic sectoral knowledge on the other hand could play an important role in ensuring development effectiveness and mitigating credit risks.

In addition to expertise, I can see three prerequisites for effective and sustainable operations of the IDB Group: cooperation, development effectiveness, and financial soundness.

Firstly, it is important to realize that many bilateral, multilateral, nongovernmental, and national actors are involved in addressing the important issues of this region. What is needed is effective coordination at the operational levels in order to avoid duplication and ensure synergy and specialization. Incorporating complementarities with the actions of other multilateral and bilateral donors and coordination in the forthcoming Country Private Sector Development Strategies is in our view a promising initiative.

Secondly, the Bank should continue to assess the impact of its operations and swiftly implement a comprehensive system to ensure and measure its development effectiveness. It is only in this way that we will know whether the Bank is on the right track when combating poverty and promoting pro-poor growth. Indeed, assessing the impact of current lending instruments should take precedence over introducing new ones. As was visible in my previous example on Dutch deregulation, first assessing the impact of present policies or instruments is the key to achieve real results.

Finally, throughout their operations the IDB and IIC need to walk a fine line between maximizing their reach and guaranteeing that the cost of capital remains sufficiently low and risks for shareholders limited. In this regard, we are pleased with the adoption of a capital adequacy framework by the IDB, which takes the risk profile of its portfolio into consideration. The newly adopted loan charges methodology is a cornerstone of IDB financial policy. It remains essential to keep IDB policies such as expanding the mandate of PRI or a possible institutional realignment consistent with this framework, ensuring the financial solidity of the Bank. In time, a similar capital adequacy framework for the IIC would be useful. We would like to congratulate the Corporation on its recent return to profitability.

As has been already made clear in a more eloquent way by both President Iglesias and our host, President Toledo, widespread poverty and an exceedingly unequal distribution of income remain the most stubborn challenges for both the countries of the region and the IDB Group. The Millennium Development Goals add to that challenge and will require the region to pull together to an even greater extent, in order to make a determined effort to reach the goals by 2015.

Private sector development, if done right and within the context of sound financial policies, can be an invaluable instrument to meet all of these challenges. But private sector development by itself is not enough, however essential it may be. The latest data, as has been stressed by many with satisfaction, show that growth has returned to the Latin American region. It is up to our governments and the IDB Group to make sure that it truly benefits all.

ADDRESS BY MS. MARÍA ANTONIETA DE BONILLA, GOVERNOR FOR GUATEMALA, ON BEHALF

On behalf of the Governments of Belize, Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua, I would like to express our gratitude to the Government of Peru and the authorities of Lima for the warm welcome and hospitality extended to us during our stay in this magnificent city. I would also like to thank the Inter-American Development Bank, and President Iglesias in particular, for their unflagging support of our countries' efforts to eliminate poverty and to help our people build a better future for themselves.

Latin America and the Caribbean continue to experience difficult social and economic conditions. Against this backdrop, Central America has not been immune to the effects of the worldwide economic slowdown, deteriorating terms of trade, and other shocks that have adversely affected the region. Nevertheless, expectations for a pickup in growth are encouraging. The progress made towards implementing structural reform in Central America is a sine qua non for higher growth rates and we are sanguine about the prospects in the immediate future.

We are firmly committed to the democratic process, the rule of law, transparency, poverty reduction, and the efficient use of resources, and are resolved to integrate our economies into the process of globalization. The political and economic costs of these processes, however, are still considerable. A stable macroeconomic framework governed by fiscal discipline continues to be a central component of efforts to achieve these objectives.

Investment in human capital, the removal of trade barriers, the privatization process, efforts to attain the Millennium Development Goals, support for microenterprise and small and medium-sized businesses, reforms and initiatives to create a more favorable business climate, and reforms to enhance the efficiency of the State are indicative of the actions under way in each of our countries over the last decade. Tepid growth in the region, though, is attributable to more than just unfavorable economic conditions. The region must also continue to strengthen its institutions, since institutional shortcomings hinder effective progress, poverty reduction, and economic recovery. In Guatemala, for example, the new administration of President Oscar Berger that took office on January 14 has been having trouble moving forward with its program because of the deteriorated institutional framework it inherited. This situation is the result of the fiscal problems left behind by the previous government and of persistent cases of corruption involving the previous administration that have cost the country millions of dollars.

The policy agenda of Guatemala's new government centers, therefore, on probity, transparency, efficiency, consensus building, and reactivation of the Peace Accords, with a focus on resolving the fiscal problems affecting the economy and on creating a setting that fosters productivity and national competitiveness.

The region clearly faces many different challenges that must be tackled in order to preserve the gains made heretofore. For instance, institutions need to be strengthened and reform consolidated in order to spawn opportunities for growth and employment.

Also, we feel the free trade agreements with countries in this hemisphere and in other parts of the world are meaningful instruments that should continue to be promoted and consolidated. In this regard, Central America has undertaken important initiatives such as the signing of the Free Trade Agreement with the United States. If the countries of Central America are able to capitalize on this opportunity, their people will benefit directly from increased investment and employment.

Another area where headway has been made is the Puebla-Panama Plan, which will help forge stronger economic and social ties within the region. The Central American countries recently introduced specific measures to facilitate the free transit of persons and goods, with a view to putting in place before long a regional customs union. All of these efforts will naturally require financial and nonfinancial support from the IDB Group.

At this year's Annual Meeting, we will be discussing institutional issues of major importance to our countries as shareholders and as users of IDB resources. I would like to mention here a few points of significance to Central America.

The private sector window was established to promote the development of small and medium-sized businesses. It is considered especially important in the region that review of the private sector windows should rest on the premise that these facilities need to be financially sound and that their shareholders are governments with an interest in development. Our region supports greater involvement by the IDB Group in private sector development and welcomes the strategy to promote the sector.

Moreover, an assessment of the private sector in small countries is essential for an efficient restructuring of PRI and the Corporation so they can have a better understanding of the needs and nature of this sector. Clearly, the objective of such an assessment must be to pursue development and complementarity with the products available in the financial systems of these countries, not to compete with them. We would like to see more assistance for small States like the Central American countries in order to broaden their access to mechanisms in support of small and medium-sized businesses.

It is our hope that the review of the IDB Group private sector windows and the problems affecting them will not be detrimental to the Multilateral Investment Fund (MIF) and that it will not be impaired by new coordinating mechanisms that could have a negative impact on its dynamic nature, assistance it provides to these countries, and its fast response. Through the MIF, the IDB Group has played a leading role in private sector development and the reforms that have spurred competitiveness. As a region, then, we would urge all of the countries represented here to join us in endorsing a replenishment of resources as soon as possible.

One issue of overriding importance to all of us here is how to assist the region's poorest countries. The shortage of concessional funding is a major stumbling block to growth and poverty reduction efforts in these countries, and this is cause for concern. That is why we believe the question of an FSO replenishment must be addressed and given the priority it deserves.

As to the financing framework, in Central America it is felt that, because the Bank is a development institution, investment programs should continue to be the cornerstone of its work and conditions should be more flexible. In our view, sector programs should continue to focus on reform to support development in the countries, based on a long-term perspective. All Bank-supported operations should emphasize development value added, leaving major liquidity concerns to institutions which have that as their core mandate.

We firmly believe that the Bank should continue assisting small economies through innovative programs such as the Action Plan for C and D countries. In our judgment, the Bank must help these countries expand their absorption capacity, where the additionality of resources is essential for reaping the expected benefits.

All that I have mentioned here touches on another crucial issue, the development effectiveness of the IDB Group's financial and nonfinancial products. We would like to express our satisfaction with efforts within the Bank to monitor the development effectiveness of its activities.

Lastly, I would like to say that the Central American countries reiterate their commitment to active involvement in all activities that help the IDB Group to accomplish its overarching objective: "the development of Latin America and the Caribbean."

In the absence of Governor Xavier Nogales, it falls to me to speak on behalf of a country that is currently experiencing a very difficult moment in its history.

The persistent economic crisis, social conflicts, and precarious political stability in Bolivia led to a change of government through a constitutional succession in October of last year.

The new administration, headed by President Carlos Mesa, has inherited a country in crisis where the three main short-term macroeconomic problems are growing unemployment, the large fiscal deficit, and weaknesses in the financial system.

With a view to addressing these challenges, the government unveiled an Economic and Social Program to the nation in January of this year, whose primary objectives are economic recovery and stability.

The approach to preserving economic stability centers mainly on a gradual reduction of the fiscal deficit. The first goal is to lower the deficit from 8 percent of GDP in 2003 to 6.8 percent in 2004. In order to achieve this target, the government has taken steps to reduce current expenditures, adopting a clear policy of austerity and seeking congressional passage of a bill creating a financial transactions tax, which already has Senate approval.

To spur economic recovery, measures have been taken to revitalize labor-intensive sectors, promote domestic industry in government procurement, and boost exports.

After taking actions to emerge from this crisis, the next most important task before the government is to ensure the export of natural gas. In light of the strong opposition to gas exports seen in October 2003, the government has had to schedule a referendum for June 2004 and draft a new hydrocarbons law to submit to Congress. A favorable outcome to the referendum and passage of this law are key to making viable the sale of gas to foreign markets, which is crucial for Bolivia's economic future.

Along with the urgent need for the kind of increased economic growth that would reduce unemployment and strengthen the financial system, it is important for Bolivia to meet the Millennium Development Goals of satisfying basic needs and reducing poverty. Working toward these goals is a responsibility shared with multilateral organizations whose support will be essential now and in years to come.

Given the weaknesses in the public finances, external credit has been a major factor in helping to contain social conflict. In this regard, it is important to underscore the Inter-American Development Bank's firm support for financing the public sector deficit at the end of 2003.

Considering the vital importance of external resources, especially those of the IDB, in the development process for the region's countries, I would like to put forward four proposals.

The first is to replenish the Multilateral Investment Fund (MIF), given the favorable evaluation of its contribution to date. In the specific case of Bolivia, MIF resources have been essential for the growth in microfinance. This replenishment should not be contingent upon institutional changes in regard to private sector lending, and it is important for more IDB member countries to join this Fund.

The second proposal is that the Fund for Special Operations (FSO) be replenished, since it has dropped by 20 percent and is expected to disappear over the next four years. Access to concessional resources is a pressing need for Bolivia given its heavy debt burden, which is why we propose that IDB Management prepare a study on replenishing these resources for a longer period of time.

The third proposal centers on the need to maximize the impact of IDB support for the private sector. For this to occur, there must be a sufficiently stable economic and political climate to attract domestic and foreign investment. In this regard, we feel that IDB lending to the private sector ought to minimize the biases that may hinder the development of domestic capital markets, channeling loans primarily toward the development of microenterprise and small and medium-sized businesses, and leaving large companies to tap the capital markets for financing.

Fourthly, we propose the appointment of a private sector coordinator who will be responsible for the three financing windows. We further suggest that credit be extended to all economic sectors.

In addition to these four proposals, it is important that the IDB maintain balance in its lending, gearing resources toward the implementation of public and private sector projects, the design of public policies—vital to improving institutions—and helping countries contend with emergencies resulting from natural disasters and political conflicts.

At the same time, it would be incumbent upon countries that receive external financing to develop monitoring systems for an efficient and effective allocation of the financial resources they receive.

In closing, I wish to express our support for President Enrique Iglesias's initiative to create the Inter-American Foundation for Culture and Economic Development. We are convinced that the promotion and support of culture and the arts will constitute a major contribution toward reducing poverty, especially in rural areas where culture can help to improve the population's standard of living. I would also like to commend and thank the Government of Peru and authorities of the City of Lima for their hospitality and their excellent organization of this Annual Meeting of the Board of Governors of the Inter-American Development Bank.

The difficult economic situation in part of Latin America and the Caribbean in the last few years, which has, in fact, been somewhat alleviated during 2003, continues to be a serious challenge for our institution; namely, to provide the adequate assistance which member countries may expect in such times, and, at the same time, not to expose the IDB to an unjustified financial risk. I wish to open my statement by encouraging the Management and the Board of Executive Directors, who cope with this challenge on a day-to-day basis, and to thank them for their efforts in this regard.

The focus of our institution on specific strategies and instruments has been constantly updated over time and adjusted to changing circumstances. In the last decade, various new strategies were developed to cope with such changes, including, but not limited to, the Enterprise Development Strategy for SMEs and the Capital Markets Development Strategy (1995), or the Financial Markets Strategy (1999). This year, the IDB embarks on a new Private Sector Development Strategy. This is an important initiative that we welcome very much, and on which I would like to focus in my remarks.

The importance of having an orientation on private sector development could not be underestimated. Despite the recent progress in stabilizing the economic situation, Latin America and the Caribbean still perform poorly in terms of growth and poverty reduction. In fact, the unsatisfactory progress in reducing poverty places the ability to achieve the millennium goals in question. Therefore, there is a need to enhance the overall development process and make it more constructive. The private sector should have a key role in any attempt to improve the development process, as has been shown by a number of studies and also recognized by other multilateral development organizations. This role stems from the large weight of the private sector in economic activity and its ability to produce opportunities for all, which means that private sector development has a high potential to contribute to a pro-poor growth process.

The most recent version of the Private Sector Development Strategy that has just been approved by the Boards of Executive Directors is, in our view, a convincing conceptual framework. Moreover, it is particularly encouraging that the strategy emphasizes the important element of improving the business climate in the region. As we know very well, the quality of the business climate is crucial for a successful private sector development process. The explicit incorporation of this element into the new strategy as a main pillar is a clear signal of the intention to increase the effectiveness of the strategy.

Given the fact that a good conceptual framework is already in place, the test of the strategy and its consequent success will now depend on its implementation. It is all the more important that in the next few months a thorough consideration will be given to some crucial issues, so as to enable the Bank to specify in operational terms how these issues will be handled. Let me point out briefly some of these issues.

One such issue is the coordination and realignment of the Private Sector Development Strategy with the public sector arm of the Bank. This coordination is required to effectively improve the business climate through proper implementation of necessary reforms by governments in the region.

A second issue is the necessary coordination required among the three private sector windows of the Bank, and probably the possible extension of this issue to the question of merging or reorganization of the various agencies.

Another issue is the risks involved in entering into certain new sectors in which the Bank does not have much expertise or capability to assess and manage these risks. Practically, the question is how these risks can be avoided. To the extent that entering into new activities proves to be necessary, a framework for a cautious and gradual approach should be worked out.

The last issue, in my opinion, is how to make sure that programs and operations of the Private Sector Development Strategy will be of a results-oriented nature. This is related to the general broad subject of development effectiveness, which has been on the agenda for quite some time. It would be very fortunate if the Private Sector Development Strategy, as a priority strategy of the Bank, could become a pilot for development effectiveness from the outset of its operations.

To sum up, these issues should receive convincing answers in order to make the implementation of the new strategy more successful. I want to encourage the Bank to move in the direction of producing such convincing answers.

Finally, I need not say that the ultimate objective of our institution is to raise the standard of living in Latin American and Caribbean countries. With this in mind, the ever-present challenge for the IDB is to identify the needs of countries in the region and to provide them with the necessary assistance. This, after all, is the fundamental reason for our participation and support of the organization. I would like to take this opportunity to praise the institution, the staff, and President Iglesias for their devotion to this demanding mission, as well as for their persistent effort to meet the Bank's goals. I would also like to join other speakers and to thank wholeheartedly the city of Lima and the Government and people of Peru for hosting this Annual Meeting in such a friendly and well-organized way.

It is with great pleasure that I address this distinguished meeting on behalf of the Government of Portugal. I would like to join the speakers who took the floor before me in thanking the Peruvian authorities for their hospitality, as well as the Bank staff for their efficient organization of this Annual Meeting.

After a period of sluggishness in the international economy, in 2003 we witnessed modest real economic growth. The outlook for 2004 for the region is encouraging, with a projected growth rate of close to 4 percent.

However, we should not forget that this positive overview also includes some elements that are cause for concern. These will require ongoing efforts by the Bank as well as by the member countries. Slow growth in per capita income in the past decade, growing unemployment, and low productivity have brought poverty rates up instead of down.

I would like to turn now to the central issue of this Annual Meeting, the private sector. Poverty reduction is the core objective of the Bank and economic growth is a prerequisite to achieving it. Growth cannot occur without a strong private sector. In our opinion, the Bank and the Corporation play a key part in developing the private sector through both investment lending and technical assistance.

We would like to commend the Bank on finalizing the Private Sector Development Strategy, which constitutes a sound foundation for preparing action plans and coordinating the various arms of the IDB Group. The final decision on the future structure must be based on a detailed analysis of the market's absorption capacity, the comparative advantages of the Bank, and all the costs involved.

We also welcome the initiative launched by the Bank to improve the investment climate. There is no doubt that sustained poverty reduction will depend to a great extent on an enabling business climate, which can only be achieved through such factors as political and macroeconomic stability, the rule of law, and adequate infrastructure and services. Improving the effectiveness of these foundations will be the challenge for the Bank and its member countries in the coming years. This work, which will have a country focus and involve coordination and joint action by the institutions involved, will undoubtedly be fundamental for the initiative to be successful.

We wish to congratulate the Management and Board of Executive Directors of the Corporation for the work they have done over the past two years. The positive financial performance in 2003, though still modest, is just one indication of the progress achieved. After a difficult period, the results of the measures taken under the 2003–04 Action Plan are beginning to be visible.

The Corporation will have to continue its efforts to improve the quality and impact of its current project portfolio and of future projects, respond more effectively to market needs and work jointly and in coordination with the other arms of the Bank Group. The lessons learned from implementation of the Action Plan, together with the recommendations of the External Review Group, should lay the foundation to devise the Corporation's future business plan.

With regard to the MIF, we are pleased with its groundbreaking operations and the good results obtained, as reflected in the outpouring of appreciation by the beneficiary countries. We have high expectations that new members will be joining the MIF.

As for the Bank itself, we are pleased to note the significant increase in the volume of both lending and disbursements to levels more in line with the Bank's financial capacity.

We must recognize that the decrease in investment lending and increase in the volume of policy-based lending is a trend the Bank shares with its sister organizations. Accordingly, in our view, greater harmonization and coordination with the operations carried out by the World Bank and the International Monetary Fund are essential in order to maximize results. Any significant increase in this type of operation should be subject to the Bank improving its capacity to assess its development impact.

Along the same lines, any diversification in the Bank's available lending instruments, along with expansion of its Private Sector Department, should be contingent on real market needs, the Bank's capabilities, and a detailed assessment of the results obtained through the current instruments.

Although we are aware of the social difficulties resulting from the implementation of structural adjustment programs, which affect above all the poorest segments of the population, we believe that the region is on the right track. Implementation of responsible macroeconomic policies and legal and institutional stability will no doubt lead to a cycle of sustainable economic growth.

The case of Brazil is a good example of reconciling reforms and macroeconomic management with social programs, in order to alleviate the adverse impact of the reforms.

I would not want to end my statement without expressing my appreciation for the Bank's work on development effectiveness, namely through its appointment of an official to head up the new unit. Actually, the impact of an institution can only be assessed if it is quantified, a very difficult exercise in the area of development. All the sectors in the Bank therefore need to make a special effort in this respect.

In conclusion, although we are aware that much remains to be done, I would like to highlight the Bank's consistent responsiveness to the crisis situation in recent years. With a clearly more positive outlook now, we would like to reiterate our support. We trust that the IDB Group, under the effective leadership of President Iglesias, will continue to devise and implement appropriate means of reducing poverty in the region.

It is a pleasure and honor for me to address this distinguished audience today on behalf of my Government. I too would like to express sincere appreciation to the Government of Peru and the people of the historic city of Lima for hosting this meeting.

Last year, Latin America and the Caribbean finally began to recover from recession and stagnation that were threatening to undermine the achievements of the structural reforms. The Bank, likewise, managed to considerably increase its lending volume. Although we would have liked to see a larger number and volume of investment loans, we acknowledge the pressing need for, hopefully, a temporary increase in emergency lending to support a fragile recovery of the borrowing members. Having said so, we are however, not disappointed with the progress made towards meeting the IDB-8 mandates. It is worth noting that lending for poverty reduction and social equity was higher than projected.

Let me now touch upon some of the main strategic issues that we find particularly important for the Bank's future focus.

To begin with the private sector issues, we note with satisfaction the approval of the Private Sector Development Strategy that constitutes an important foundation for potential private sector enhancement. While we would like to commend the Management for the work done so far, this is still far from being a "mission accomplished". With the strategy now in place, we would like to encourage the Management to work out the time-framed implementation plan without delay. Given its sensitivity and complexity, we do not expect it to be perfected in the relatively short term. We believe, however, that under the guidance of the recently established Ad-hoc Committee it could be elaborated in details through a comprehensive dialogue based on a solid analysis.

Acknowledging the demand for greater flexibility, expressed by the borrowing members, and being aware of the headroom for private sector lending, we too are ready to consider the possibility of gradually extending the private sector mandate. A word of caution, however, is necessary. In principle, we would not oppose extending this mandate, provided that underserved and less-developed countries—particularly poor and small ones—are given priority and the poverty reduction focus of projects is ensured. We believe that in keeping with the intention to corroborate the country focus of the Bank's operations, country-specific private sector development action plans for such countries would be warranted first.

It goes without saying that in the course of transforming the private sector operations toward enhanced development impact, both coordination among three private sector units as well as that between the private sector units and public sector departments is essential. Likewise, the Bank should further step up its cooperation and coordination with sister institutions to be able to fully utilize its comparative advantages.

Turning now to another equally important strategic issue, we were pleased to learn from the report on development effectiveness that the Bank made progress toward strengthening measurable results in the past year. Though we are aware that streamlining of management for results is a continual process rather than a one-time mission, we wish that more had been achieved. Clearly, there is still a lot to be done. Transformation of the Bank's culture into a result-oriented one can not be done overnight and can not be achieved successfully unless the sense of ownership is shared by all the Bank's departments and, equally important, by all the borrowing country governments. In this regard, we would like to welcome the appointment of the Chief Development Effectiveness Officer for coordination of activities in this area. We welcome his commitment to prepare the Mid-term Action Plan by this summer, which we are awaiting with great interest.

The Bank must continue to be a flexible institution adequately responding to the needs of its borrowing members. It should be capable of providing an adequate toolkit of instruments and a mix of borrowing modalities. In so doing the Bank should, however, not lose sight of the long-term objectives of poverty and inequality reduction. Given its relatively modest size in contrast to the development finance needs of the region, the Bank can add value only if its support is provided in a developmentally effective way. In our view, ideas to increase fast-disbursing loans or introduce new instruments should be considered from this perspective rather than from the short-term needs of liquidity provision. Since the investment loans have proven the capacity to create developmental impacts in terms of poverty reduction, which is at the heart of the IDB mission, we would like to urge the Management to step up its efforts in improving this lending modality first. We of course remain open-minded about considering a cautious increase of the Policy-Based Loans once they have demonstrated their ability to create verifiable developmental impacts and are approved in a coordinated manner with the World Bank and IMF programs.

I would like to reiterate the commitment of the Republic of Slovenia to the Bank. Let me conclude by expressing our appreciation to the staff and the Management of the Bank and especially to you, President Iglesias, for your firm leadership.

In conclusion, I wish that as the result of well-executed social sector programs in Peru, the poor of this country could also experience some of the unforgettable events we were exposed to in the last three evenings.

Let me begin by expressing my government's appreciation to the authorities of our host country Peru and the city of Lima for their generous hospitality in hosting this Annual Meeting. I also want to thank the IDB Management and staff for the professional and high-quality preparations of the meeting.

The fact that the general economic outlook in the region has shown signs of improvement since the last Annual Meeting is encouraging and something that should strengthen our drive for further and stronger progress. We are in a good position to continue this work, because at the global level there is an unprecedented consensus on where we should aim our development efforts. The Millennium Declaration and the Millennium Development Goals have established the set of objectives that we are to achieve. I am happy to note that the IDB's Management has again indicated the full commitment of the IDB Group to these objectives. Nevertheless, a lot of work for all of us remains to be done, in order to put into concrete action—particularly at the country level—the pledges and commitments made at the global level.

President Iglesias stated in his remarks to the meeting of the Committee of the Board of Governors here in Lima that "Latin America and the Caribbean claim the sad distinction of having one of the widest disparities in income distribution and opportunities, as well as in access to health, education, water, sanitation and electricity services." We believe that this is a message to be taken seriously. The "global deal" made in Monterrey at the Financing for Development conference in 2002 included commitments and responsibilities for all countries. All countries have pledged to take full ownership of their own development and to seriously commit to the principles of good governance, democracy and human rights. And the international community has committed to supporting developing countries in this process, by means of investments, trade, development assistance and debt relief when appropriate.

The recently published report by the World Commission on the Social Dimension of Globalization, established by the International Labour Organization and co-chaired by the Presidents of Finland and Tanzania, made a strong point on the need to rethink globalization. The report emphasized that instead of focusing on the preoccupation with markets, the emphasis has to change to preoccupation with people. In practice, this would mean more emphasis on social dimensions of globalization. The report further emphasized that each state should "ensure high and stable economic growth, provide public and social protection, raise the capabilities of people through universal access to education and other social services, and promote gender equity." That, the report states, is also a precondition for fair globalization.

The forthcoming summit in Guadalajara between the European Union and the Latin American and Caribbean countries will also enhance the commitment of these two regions to development in Latin America and the Caribbean. We think that the importance of President Iglesias' above-stated argument on more equal income distribution is illustrated also by the fact that social cohesion will be one of the central themes of the summit in Guadalajara. And to add to this, when an institution such as the IDB that should be and is combining the pursuit of economic growth with emphasis on equity and social development, we believe that gender equality must come in as an integral, cross-cutting element in all activities.

One of the implications for the IDB of the importance of all this is, in our opinion, an even stronger country focus in operations. Progress made on issues such as harmonization, cooperation and coordination with other actors at the country level is absolutely crucial for the success of the Bank. Also, working very closely with the governments and other players in the country environment, especially civil society, will enhance the results of operations. The Bank needs to fully align its activities with national strategies, be they poverty reduction strategies or other nationally designed and owned development strategies. We are happy to note that the IDB's country strategies have been evolving in this direction, but would like to call for continued efforts to enhance this development.

Let me turn to some specific organizational challenges that the Bank as a development institution will need to successfully deal with in the very near future.

First, Finland is fully backing the Bank to support private sector development in the region. A well-functioning and strong private sector is not only essential for development within a country, but is also the basis for developing foreign trade opportunities. In the case of the Latin American and Caribbean region we recognize the active role of the Bank in trade issues at the regional level, and capacity-building efforts at the country level. We would welcome a more proactive role for the Bank in deepening the interregional trade arrangements in the spirit of the Doha development agenda in order to maximize the benefits of trade for poverty reduction. The importance that my country attaches to trade as an engine for development is illustrated by the fact that last year Finland decided for the first time to combine the ministerial responsibilities for foreign trade with the responsibilities for international development cooperation in one ministerial portfolio. To have one minister in charge of both trade and development is an example of our response to the demands for greater policy coherence.

With this line of reasoning, Finland welcomes the recently approved Private Sector Development Strategy. We also strongly support the proposal to appoint a high-level official to begin looking at all activities of the various parts of the IDB Group that deal with the private sector in a coordinated manner. It is indeed necessary that the IDB as a whole will be able to contribute more strongly to this sector. At the same time, we emphasize that as a development institution, the IDB's activities related to the private sector need to be strongly linked to the institution's overarching mission to support long-term, sustainable economic and social development, and also to be aligned with national development strategies and the Bank's country strategies.

Second, we continue to underscore the importance of the issue of development effectiveness. We recognize that genuine progress has recently been achieved in the Bank's approach and operations and we wish to commend President Iglesias for his strong personal commitment in taking this issue forward. Encouraged by this progress, we are looking forward to seeing further consolidation of the issue within the Bank, to adherence to the implementation timetable proposed in the action plan, to the preparation of a single development effectiveness framework for all Bank operations, and eventually to the IDB becoming a leader on development results in the region.

Third, there is the issue of new lending instruments and operational policies. I wish to emphasize, again, the role of the IDB as a development institution. All activities and instruments need to have a strong and direct link to poverty reduction and the Millennium Development Goals. In our opinion, the IDB should adhere to the agreed lending framework for 2002–04. We will, naturally, be ready to participate constructively in the forthcoming discussion of a new multiyear framework for the year 2005 and onwards.

Fourth, I believe that the issues of internal coordination, as well as transparency and accountability in the IDB Group are essential for the IDB to use its resources in the most effective way possible, and to be able to demonstrate this also to the outside world. Internal coordination means strengthening cooperation and coordination between all levels of the Bank Group, at the strategic level and at the operational level in the countries. Significant advancements have been achieved on transparency and accountability, for example, in the form of the new disclosure policy and the Independent Investigation Mechanism. It is the duty of all of us to follow up on this, to make sure that the policies and mechanisms are fully visible and reflected in the reality of the Bank's day-to-day work.

Let me conclude by stating Finland's appreciation of the IDB's commitment to sustainable economic and social development in the Latin American and Caribbean region. Finland continues to appreciate the opportunity to be a partner of the IDB for the benefit of this region.

First of all, let me begin by thanking the Peruvian authorities and the city of Lima for hosting this year's Annual Meeting and for its warm hospitality expressed to all of us.

The general economic outlook for Latin America improved during the past six months and we can cautiously hope that the worst is behind us. Yet the effects of the recent recession and in certain cases outright crises will be with us for some time ahead. The economic recovery for the region as a whole is continuously modest and several downside risks still prevail.

In the light of achieving the MDGs, including reducing poverty by half, we note with deep concern that poverty rises and income inequality grows. Poor economic growth during several years, increased unemployment and widening wage gaps contribute to social distress and discontent in parts of the region. Moreover, in several countries we see a decline in confidence in governments' ability to tackle issues such as governance, corruption, social exclusion and inequality. This is serious in that it may many times result in a weakened trust in democracy that could ultimately lead to political and social unrest as we have seen recently.

The Bank is uniquely placed to play a significant role in the development of the region, through its knowledge, its experience, its large financial resources, its leverage and not least the legitimacy it derives from its regional character. The Bank must continue to pursue its mandate as a development institution by supporting the countries in the region to achieve sustainable economic growth, enhanced social equity and gender equality.

In order to fulfill this role, the Bank must continuously reinvent and assess itself, that is: its structure, its internal practices and its modus operandi, to ensure that it remains relevant. In that context, Sweden wishes to address certain issues that have been discussed during the past few days: development effectiveness, private sector development and the Bank's future lending framework.

We welcome several of the Bank's initiatives with regard to strengthening the development effectiveness agenda of the institution, such as the appointment of the Chief Development Effectiveness Officer, increased participation from country office staff in project formulation, improved indicators for results and evaluation, as well as the Bank's involvement in the international roundtable on managing for development results in Marrakesh earlier this year.

However, a successful and full implementation of the development effectiveness agenda requires substantially more and, most importantly, a consistent focus on measuring and monitoring the results achieved by the Bank. A sustainable impact on the Bank's operations and activities calls for nothing less than a cultural change. It is therefore crucial to establish the incentives that promote a more results-oriented culture within the institution, which in turn would encourage a broader ownership. Securing necessary human and financial resources for the Development Effectiveness Unit is crucial.

Closely connected to increased development effectiveness and ownership is the participation of the IDB in harmonization and coordination processes. Particularly important is the Bank's alignment with national development strategies and coordination initiatives at the country level. This reduces the demands on governments and enhances ownership, transparency and accountability. Holding the government directly accountable for the national development strategy reduces the risk of conflicts with regard to the government's accountability to its domestic constituency on the one hand and to development agencies on the other.

We are pleased to report that several, successful coordination and co-financing projects have been set in motion between Sweden and the Bank during the past year; one of them being the fiscal reform processes in Central America where the governments and several donors have been working jointly in the development of operations, drawing upon respective experiences and comparative advantages.

A monitoring system based on result-oriented indicators is highly dependent on extensive and reliable data. In-country capacity building and improvement of statistics, accounting and reporting are therefore of great importance with a view to strengthening the country's own monitoring capacity. Indicators should be extracted from the national development strategy, chosen by the borrowing country, aligned with the MDGs and harmonized with other donors in the country. We welcome the Bank's recognition and urge the IDB to continue cooperating with other MDBs and the UN in this work to build on best practices.

The private sector has an obvious role to play in generating the necessary growth needed for reducing poverty and increasing equity. A stable and secure environment is essential to stimulate business development and not least to attract both foreign and domestic investment. Stable institutions play an indispensable role here of which a sound and transparent legal system is vital.

We applaud the approval of a coherent private sector strategy for the IDB Group and we urge that continued measures are taken to improve and strengthen coordination within the entities. It is critical that a high-level, private sector management position, externally recruited, is given a clear organizational mandate and responsibility to develop and secure implementation. Ensuring that the private sector strategy does not lose alignment with the overall objective of the Bank, contributing to increased development and poverty reduction in the region cannot be stressed enough. Increased lending to and investment in private sector entities through the IDB is not an end in itself. Operations with the private sector should only be seen as a means to achieve the overarching development mandate of the IDB.

We certainly welcome that the Regional Public Goods Initiative was recently approved, and look forward to further discussing the concrete actions within this promising initiative. However, we are somewhat concerned with the Bank's definition of Regional Public Goods, which we find rather broad. We therefore encourage proposals that give predominance to public goods requiring broad international cooperation, and are key international public goods, instrumental for alleviating poverty in the region, and of common interest for an equitable and sustainable global development. These goods may include efforts to address problems such as environmental degradation and epidemiological diseases.

Finally, in order to meet the changing needs of borrowing countries in the most appropriate way, it is important to continuously review the lending instruments of the Bank. However, we firmly believe that we must first evaluate the existing framework and lessons learned. This will undoubtedly establish a sound basis for forthcoming discussions on a new multiyear framework starting in 2005, which we expect to be accompanied by reliable and measurable performance indicators. It must be ensured that increased lending flexibility neither clouds the Bank's objective of efficiently contributing to improved well-being for the poor, nor jeopardizes the Bank's financial strength and soundness. This cannot be stressed enough.

In closing, let me point out that Sweden feels that much has been done and we stand behind the overall thrust of the recent initiatives and reforms President Iglesias has set in motion. We must now build on this momentum to ensure that the Bank is able to continue playing a significant role in helping countries in the region face their development challenges, and set them on the path to attaining the Millennium Development Goals.

ADDRESS BY MR. APOLINAR VELOZ, TEMPORARY ALTERNATE GOVERNOR FOR THE DOMINICAN REPUBLIC

On behalf of the Dominican Republic, its government, and its President Hipólito Mejía, I would like to say how pleased we are that the city selected for the work of the IDB and IIC Boards of Governors is Lima, a city of unique architecture that has justifiably been declared a World Heritage Site and, above all, is a city of friendly, welcoming, and warm people.

I would also like to take this opportunity, on behalf of my country, to thank the IDB and its president, Enrique Iglesias, for the timely financial and technical assistance that has helped to mitigate the negative impacts of the financial crisis affecting our country. The IDB rose to the task and, for this, the Government of the Dominican Republic wishes to express its gratitude publicly. In my brief address, I shall make reference to the activities being carried out by the current administration to put the Dominican Republic back on the path of stability and growth, and to do so against the backdrop of the global economic setting. I will also comment upon a number of IDB programs that we regard as vital for development of the region.

Despite the significant slowdown in the global economy in 2001 and the slow reversal of this situation in 2002, recovery in the past year has been vigorous, driven by growth in the U.S. economy, a rebound in Japan, and vigor in most of the East Asian countries. This, combined with the return to growth in Europe and robust performance of the stock markets, makes for a very promising outlook for 2004.

The global economic recovery in the latter half of last year was conducive to revitalized trade, which expanded at a rate comparable to that of 2002. However, this growth fell short of compensating for the sharp contraction in 2001 and also was shy of the high growth rates recorded in the 1990s. But in the economies of Latin America and the Caribbean, exports increased, not only in volume but in price terms, and became the most dynamic factor in demand, enabling the region to achieve a substantial trade balance surplus and to reactivate growth.

Alongside these factors, however, there is serious concern in the region with regard to the path of foreign direct investment (FDI), which has continued to decline for the fourth consecutive year. In 2003, FDI dropped by 25 percent, to a level below the annual average for the period 1990–2002. It is essential to improve this performance, as such investment constitutes a significant supplement to the external saving needed to increase gross capital formation in support of growth and development.

While the external sector indicators (tourism, national and export processing zone exports, and remittances) have rebounded considerably from last year, the Dominican economy failed to expand because of the impact of the financial crisis triggered by the collapse of one of the major banks in the financial system, as well as assistance to maintain liquidity in two others. Such financial assistance to rescue depositors generated uncertainty, as reflected in the loss of confidence on the part of economic agents. This led to, among other explanatory factors, a massive repayment of private debt in foreign exchange, which had already been declining, and in turn accelerated the pace of currency depreciation, thereby increasing inflation and interest rates, a situation that constituted a disincentive for domestic investment and demand. As a result, the Dominican economy, for the first time in more than a decade of high growth, experienced a contraction of roughly 0.4 percent in 2003.

Even though the government now in office is in the midst of an electoral campaign, it has made it clear that macroeconomic stability is its fundamental priority. This responsible attitude is being well received by economic agents and by the international financial community. To boost the credibility of the new stabilization policies being implemented and their financing, the Dominican Republic signed a stand-by arrangement with the International Monetary Fund (IMF) in August 2003. The aim of this arrangement is to strengthen regulation of the banking system and ease exchange and inflationary pressures. However, the government's decision to purchase shares of Unión Fenosa, the owner of the power distributors Edenorte and Edesur, prompted the suspension of the first review of the program until a panel of international experts could evaluate the fiscal impact of this transaction. Upon completion of this process, and after an intense analysis of macroeconomic conditions with the technical team from the IMF, in mid-February 2004 the IMF Executive Board approved the first review of the arrangement.

The arrangement required the enactment of various laws in support of the program and of governance, which has been done. It is anticipated that implementation of the stabilization program will enable the Dominican Republic to weather the crisis and return to the path of growth with macroeconomic equilibrium that charac-terized our economy over the past decade.

It should be noted that, within the program, a balance of payments financing gap of US$320 million is projected. While such a gap implies that the country is facing a temporary liquidity problem, it is not suggestive of a solvency problem. With a view to closing this gap, financing has been requested from multilateral organizations. Another option considered is Paris Club debt restructuring of 2004 maturities and outstanding payments from 2003, a decision which constitutes part of the IMF arrangement.

With strong support from the International Monetary Fund, the Inter-American Development Bank, and the World Bank, the Dominican authorities are now engaged in adopting the measures contemplated in the arrangement, in particular those relating to institutional strengthening of the Superintendency of Banks and the follow-up objectives of improving bank regulation and supervision, enhancing transparency, and fully categorizing its operations in the manner currently being implemented by the rest of the financial system. This is being done openly, and has helped to boost the confidence of economic agents, the immediate results of which are reflected in the appreciation and stability of the exchange rate in recent weeks.

In the fiscal area, the government's objective this year is to achieve a primary surplus of 1 percent of gross domestic product (GDP), through an increase in taxes and a reduction in expenditure on the order of 2 percent of GDP. The funds made available by the debt renegotiation with the Paris Club will be used to reduce the quasi-fiscal deficit, as calculated in accordance with the IMF arrangement. A monetary policy consistent with fiscal policy has been based on restricting the growth of the monetary aggregates by boosting the interest rates on the Central Bank's financial instruments.

In recent years, and particularly after the crisis referred to above, there has been an increase in the support extended to the Dominican Republic by the Inter-American Development Bank in sectors such as education, agricultural reform, and modernization of the State. This entailed the timely, significant, and rapid approval of loans for social reform and consolidation of the financial system; these loans were disbursed at a time when the Dominican Republic was most urgently in need of external resources in order to meet its international commitments. Special mention should be made of the loan to finance the Financial Sector Consolidation and Reform Program.

We are pleased to note the approval of the IDB strategy for financing private sector projects. We also believe it extremely important, as soon as circumstances permit, to expand the activities of the Private Sector Department to encompass other productive sectors in the economies of the region, and tourism in particular.

We reaffirm once again our support for a replenishment of the resources of the Multilateral Investment Fund (MIF) and the establishment of an action plan for the immediate future, given the important role that these funds play in reforms and in private sector expansion. We further support the actions aimed at improving development effectiveness, and we support the increase in IDB financing for microenterprises and small and medium-sized businesses with a view to meeting the Millennium Development Goals. There is also one other factor of particular importance for the region: the fourth consecutive year of decline in foreign direct investment in the region. Accordingly, we support the IDB's intensification of investment lending in order to offset, to some extent, this pronounced decline, which substantially limits the levels of gross fixed capital investment required for the region's growth and suggests the need to study the possibility of increasing the resources for sector loans and policy-based loans.

The IDB has worked extraordinarily hard to serve as a catalyst and source of support for regional initiatives to open trade and achieve economic integration. Integration is one of the IDB's goals, and it should move forward with its efforts in that direction daily. The Dominican Republic is committed to making efforts to adapt its public and private institutions to the various requirements emerging from the integration processes in which we are engaged. Consequently, the country will continue to need support from the IDB in these areas.

This assistance would be timely inasmuch as the Dominican Republic has signed a free trade agreement with the United States that has enabled us to join the U.S.-Central American Free Trade Agreement (CAFTA), opening up new prospects for trade and allowing for greater insertion of the Dominican economy into the North American market. These new possibilities should be reflected in a vigorous boost in the production of tradable goods intended for this megamarket.

Finally, we wish once again to thank the IDB, and President Iglesias in particular, for the rapid and fraternal response to our requests made in difficult times, especially in the past year when the support received was of vital importance. This fraternal mission and capacity of the IDB, which stands ready regardless of whether the calamitous circumstances result from natural disasters, external economic shocks, or domestic crises, further underscores the strategic function of an institution which we should all regard as a source of pride.

We would like to share our thoughts and ideas with you today as representatives of Latin American and Caribbean youth: the young entrepreneurs in the social and economic sector selected by the IDB to take part in a seminar on "Latin American and Caribbean Social Capital in Action: Young Entrepreneurs and Volunteerism."

Young people have a strategic role to play in development and building social capital. We are committed to greater social equity and inclusion, encouraging active citizenship, and working toward social justice in the region with ethics as the cornerstone.

The scourge of poverty and exclusion still afflicts our countries, affecting primarily children, young people, women, indigenous peoples, and those of African descent. That being so, our commitment to change emphasizes full and active citizenship as an extension of our Latin American and Caribbean identity.

We know this will require a new culture of citizen participation that reinforces sustainable development models and fosters collective leadership.

Youth volunteerism has clear potential to support the social integration process through development-oriented policies and programs in the region. Volunteerism, then, must be a priority focus of social investment strategies.

The region's youth face steep challenges: unemployment, poverty, a lack of access to quality education, little say in decision-making processes, the digital divide, and environmental degradation. These are just a few of the areas urgently in need of attention. Young people are ready, willing, and able to take on the leadership role that the region's development demands.

To do so, we need the strong and steadfast support of all development stakeholders.

We call upon leaders in the public sector to:

- invest strategically in youth;
- build into government policies the active and strategic role that young people play in development;
- promote volunteerism and youth entrepreneurship as tools for building social capital; and
- encourage young people to take part in policy design, implementation, and evaluation.

We call upon civil society to:

- strengthen networking opportunities, so that young people can share experiences and make the most of their efforts and resources;
- get actively involved in the design and implementation of youth development programs and policies;
- foster consultation and dialogue with social agents working for development;

- introduce monitoring and evaluation mechanisms, to clearly determine the impact of certain practices on the community; and
- make organizations more transparent in terms of process, outcomes, and resource management.

We call upon the private sector to:

- actively engage young people in their economic and productive activities;
- step up technological research and development, so that it reaches more of the population;
- give young people opportunities for training and work experience;
- strengthen socially responsible practices within firms, opening and supporting avenues for youth participation; and
- enter into multisector strategic partnerships to support innovative youth initiatives.

We call upon international organizations to:

- support the youth development efforts of governments, civil society, and the private sector;
- provide technical and financial assistance to develop youth policies and programs;
- ensure that social investment in youth is as effective as possible by making best use of resources and setting up transparent mechanisms for allocating them;
- coordinate work with other international organizations active in the region, to promote a positive image for young people; and
- facilitate the exchange of views, know-how, best practices, and lessons learned on youth-driven initiatives.

We are confident, therefore, that the Bank's Board of Executive Directors will welcome the proposal put forward at the seminar's Closing Session by Mr. Enrique Iglesias, President of the Inter-American Devel-opment Bank, in relation to the possible establishment of a youth venture fund.

Young people are the future. But we are also the present. We are you, your children, your most enthusiastic employees. We are prepared for action. Through our daily commitment, we have shown that we can make Latin America and the Caribbean a place where all our dreams of social equity, justice, and solidarity come true.

Now, more than ever, we have the knowledge, the means, the desire, and the strength to make it happen. The time has come, and change is within our reach. The future is now.

ADDRESS BY MR. ENRIQUE V. IGLESIAS, PRESIDENT OF THE INTER-AMERICAN DEVELOPMENT BANK AND CHAIRMAN OF THE BOARD OF EXECUTIVE DIRECTORS OF THE INTER-AMERICAN INVESTMENT CORPORATION

We have come to the end of this important and historic meeting in Lima. My first words are ones of thanks to President Alejandro Toledo and his government for their very warm welcome and all the support they have given us in making this meeting a success. In particular, I would like to thank the Chairman of the Board of Governors, Minister Pedro Pablo Kuczynski, a friend of the Bank's and my own, in addition to everyone who made such great efforts to further the activities of our Annual Meeting. We know what it takes to organize these activities, in terms of time and hard work. Our hosts have done it very well, as the Governors and delegates have unanimously agreed. Efficiency has prevailed here and, above all, warmth, which is highly appreciated.

I would also like to thank the Minister of the Interior for the commitment and professionalism with which the security needed for the normal pursuit of our activities was provided. I also thank the mayor of Lima, with whom we have a relationship of very close cooperation, and the mayor of San Borja who gave me, as representative of the Bank, the keys to this important locality and was our host here in his district. We thank the mayor of San Isidro as well, who inaugurated the Paseo de las Naciones on the occasion of our meeting, an event we will always remember as a symbol of this city's hospitality.

My appreciation also goes to the Director of the Museo de la Nación for the opportunity to hold this meeting in a museum. I am very glad of it. Culture is a highly important factor in the life of nations. Development is more than economic, more than social, and even more than political: it is spiritual self-realization. Therefore we call for recognition of the cultural foundations of this country, which has millenary cultures that are mirrored in its traditions and way of life. This brings us closer to the magnificent reality of the history of this great country. I say this because the Bank has always respected cultural values and I hope that we will bear them in mind even more in the future.

Attended by 7,000 people, this meeting was the largest in our history, which has left us pleasantly surprised. To a large extent this reflects the extraordinary attraction of this beautiful and historic capital of Peru.

It is difficult to summarize the activities that took place over these last few days, including the seminars that preceded the meeting. The Governors participated actively in them. Ten points can be highlighted from the discussions during the last three days, five of them related to Bank policy and the others to Bank governance. The Governors will soon receive, through the Board of Executive Directors, the particulars of the main comments of each delegation and a written version of my remarks.

The first main general policy message referred to the economic climate, which was stressed in the Inaugural Session by President Toledo, the Secretary General of the OAS, and the Executive Secretary of ECLAC. This meeting has taken place at a very important time in Latin America and the Caribbean, when all indications are that we are emerging from the recession and beginning to grow again. The Governors mentioned this as something very important: Latin America is beginning to grow again and this opens up opportunities, with the necessary provisos. It is growth subject to the test of time and the vicissitudes of the international situation. But it is important to realize that growth offers a platform for consolidating the gains of the past, addressing shortcomings and, above all, building defenses in our countries to contend with future cyclical downturns. It is also the right moment to promote efficient social development. We are at a very special juncture that arouses prudent, cautious optimism and calls for our best skills to manage the recovery well in the coming years.

The second important message sent by the Governors refers to the need for any adjustments made to also attempt to reduce the volatility and vulnerability of our economies to the international cycle. The challenge is to promote our own development strengths and not to depend exclusively on external factors. And by our own strengths, I mean those intrinsic to the countries and those stemming from regional cooperation. In Latin America and the Caribbean, this is a vigorous source of economic stimulus that should be exploited. The Governors urged the Bank to make a new contribution to combating the recessive effects and instability of the international economic situation. This essentially implies modernization of the Latin American economies. There is no alternative in today's world; we need to compete, as the Governors mentioned in their addresses. This means to open up unfalteringly to international competition, with the risks that implies, making the most of the benefits and trying to reduce the costs inherent in these policies.

The third message that emerged from the Inaugural Session, and which was later reiterated by the Governors, refers to social issues. Social problems continue to be of concern. We are concerned about the aggravation of poverty, which has occurred despite reforms and economic growth. We continue to be concerned about inequality in Latin America. Unemployment has risen to high levels, the highest since the crisis of the 1980s. And, of course, we continue to be concerned about problems related to exclusion, which has deep ethnic roots in Latin America. Consequently, social issues continue to be the core objective of policies. All the Governors placed special emphasis on this great task that our actions in Latin America and the Caribbean must accomplish. The Bank has been committed to social matters from the beginning. Fifty percent of its operations focus on social development and therefore this message, which was reiterated over and over again by all of you, is clearly a fundamental mandate—a seminal one—for the presence of the Bank in Latin America and the Caribbean.

A fourth message sent by President Toledo and the Governors refers to the United Nations Millennium Development Goals, endorsed by all the governments in the United Nations system. They bind us all. The Millennium Development Goals are economic, social, and international, particularly in the area of trade. They are the key reference points for the Bank's relations with its member countries and should be given special consideration in the preparation of country action programs. Our next meeting in Okinawa will focus on an analysis of progress towards those goals in the middle of this decade and the positive and negative prospects for attaining them, based on the status of our economies.

The fifth message of note referred to policies for the development of economic infrastructure. In the Governors' discussions and in the seminars preceding the meeting, it was made clear that we are facing a large infrastructural deficit. Investment has fallen in recent years, including investments in productive and social infrastructure, which could become a serious obstacle to future economic growth.

In this regard, the importance of investing in infrastructure as a countercyclical element and of mobilizing domestic savings and resources was pointed out, and the role of infrastructure in deepening the integration of Latin America and the Caribbean was also emphasized. I recall that just a few months ago, a meeting of the Heads of State of the Rio Group was held in Cuzco, where the central topic of discussion was the need to increase investments in infrastructure, with the Bank being asked for more vigorous support in this area. All this illustrates how this issue has been at the heart of the debate.

Eleven South American countries signed the Letter of Lima, which pointed out the need to adjust the treatment of investments in fiscal accounts. This discussion made it possible to emphasize that investments in infrastructure have a different fiscal impact from other expenditures, and therefore they should be treated differently by international agencies, particularly the International Monetary Fund. The governments that signed the Letter of Lima, and undoubtedly all the rest, are concerned about the weakening of the Bank's actions in the field of infrastructure, which we know very well reflects the lack of counterpart resources on account of the scarcity of fiscal funds. They call for the accounting rules for spending on infrastructure to be revised and for multilateral lending agencies, particularly the IMF, to allow for differentiated and special treatment of such spending, inviting those agencies to reflect this in their policies. This subject has been highlighted on several occasions by the Heads of State, particularly by President Lagos of Chile, President Toledo of Peru, President Lula of Brazil, and President Kirchner of Argentina. There is clearly a demand for action in this field, as stated in the Letter of Lima to the international agencies.

These are the five key elements highlighted by the Governors, which are aimed at the policy of the Bank, as an economic and social cooperation agency. As for matters touching on the workings of the Bank from within, which was the other phase of our meeting, four issues were highlighted here in particular.

The first has to do with the private sector. As you know, the Bank has been working with the private sector for many years and we have different entities devoted to this area. In recent years, we have looked carefully at the most effective way the Bank can organize to work with this sector. Minister Kuczynski chaired an External Review Group, which issued a series of recommendations that the Board of Executive Directors has been examining in recent months. Now we can add the approaches arising from this meeting, which I will summarize below.

First, broad support was expressed for the Bank's strategy for private sector development, which is viewed as a key factor for giving impetus to our economies. It is therefore important to implement the strategy quickly.

In this regard, broad support was expressed for the Bank's initiative to improve the private business climate in the region, a task that will be led by the Executive Vice President. Our action to improve efficiency also received support, including the creation of the post of a high-level coordinator. This initiative will be discussed by the Board of Executive Directors.

Support was also expressed for the proposal to step up Bank action with respect to small and medium-sized enterprises (SMEs). We have been pioneers in promoting their development, and even pioneers globally in the development of microenterprise. The Bank, under the direction of my predecessor, Mr. Antonio Ortiz Mena, began to work with microenterprise three decades ago. This activity should be given more emphasis, particularly after the Declaration of Nuevo León, signed by our member countries in the region. In the declaration, they asked us to triple Bank support for SMEs in the coming years and that is what we propose to do. In this discussion, the Governors expressed their concern regarding the institutional form that the Bank's support for the private sector takes. Some Governors supported the External Review Group's recommendation to merge all the Bank's private sector windows—the Inter-American Investment Corporation, the Multilateral Investment Fund, and the Private Sector Department. Others had doubts. The matter will be examined in greater detail by the Board of Executive Directors in the coming months.

In addition, firm support was expressed for the Multilateral Investment Fund (MIF), which has proven to be a valuable tool for Bank cooperation with the governments. Great support was expressed for replenishing the resources of the MIF, which will be the topic of discussion at a meeting with the Governors next July.

The second issue referred to the flexibility of the Bank's instruments—a highly important subject that the Board of Executive Directors has been examining intensely. The Board has worked in close coordination on this issue, discussing various aspects. One concern is the failure to use our full lending capacity. This suggests that the problem is not just the lack of fiscal resources, which means that there is much to gain from examining the flexibility of the instruments at our disposal. The Governors expressed their concern over the need for an effective evaluation of what has been done until now, particularly in the area of policy-based lending. During the discussions, several questions were raised that I believe are going to guide the debate. First, what is the appropriate mix of investment loans, fast-disbursing policy-based loans, and emergency loans? What should the internal conditions in the country be like to use this mix of loans? And last, how can we analyze the development effectiveness of each type of loan? It is not a matter of having more instruments just for the sake of having them, but of improving the Bank's capacity to cooperate and efficiently apply its resources.

The third issue had to do with the development effectiveness of our cooperation—an old topic in these forums that has become very important again in recent years. I think that the Governors appreciate the efforts made by the Bank's Management in this area. It is noteworthy that the Governors have mentioned the need to establish a great partnership between the Bank and the countries to improve efficiency in the use of the institution's resources, which signifies support for the work plan that the chief of the Bank's Development Effectiveness Unit is to present this year.

Lastly, the topic of institutional governance, where the efforts being made in the areas of information disclosure and institutional transparency, with the establishment of the Office of Institutional Integrity, have been recognized.

This, in short, is what we believe emerges from the views expressed by the Governors on policy issues and the Bank's performance. They are the main guiding principles that emanate from this event in Lima.

I would like to turn now to another component of these meetings. Years ago, we began to hold seminars at our meetings to look at specific topics of interest for Latin America. Academics, technical experts, policy-makers and representatives of civil society participate. On the occasion of this meeting, five seminars were held last week, all on highly topical issues.

One dealt with the subject of governments and banks, and examined the role of the State in the banking sector through the public banks; actions to address crises; and the results of experience with government financial support for the banks.

A second was on infrastructure investments, a responsibility of both the public and private sectors, and the need for new financial structures to facilitate the provision of public and private funds and the strengthening of partnerships, which are becoming increasingly important in Latin America.

Another seminar was entitled "New Frontiers in State Reform". This area was recognized as a great challenge facing Latin America today, perhaps the most difficult reform, since in addition to reforming the public administration, it is also necessary to reform policies for the consolidation of democracy, for the functioning of democratic institutions, for the strengthening of governance. Reinventing the State was discussed, as was reinventing a welfare state that takes into account the needs, potential and limitations of the region.

The seminar on City and Marginality was attended by representatives of the municipality of Lima and the mayors of several important cities in the region, who participated actively. Ideas were shared on how to reach the sectors bypassed by development, which now include a large part of Latin America's population, having grown with the rapid urbanization in the last 20 years. The analysis of this issue emphasized that things can be done, as illustrated by experiences in Peru, Mexico, and Brazil. The municipalities are playing a very important role in this task, thanks to their direct contact with hitherto bypassed zones and their wealth of experience in mobilizing resources, which is often difficult for central governments to do. This seminar taught about dealing with poverty, marginality, and violence in today's difficult times in Latin American cities.

The last seminar dealt with the topic of young entrepreneurs and volunteerism. How could I put it better than the young people's representatives have? We thank them very much for their presence and for their strong, constructive, and fresh message. It does us all good, particularly those of us who are no longer young but who are motivated by the same spirit. This seminar dealt with the many facets of the subject. In Argentina and Brazil, volunteerism accounts for about 2.5 percent of the national product. It is very important in Latin America to talk about these things, which are above and beyond current issues, but which form part of social life.

The Bank also held round tables on topics such as technological innovation in agriculture and remittances.

The host country also organized very interesting seminars. One, organized by the Peruvian University of Applied Science and AID, was on trade integration. ALIDE and COFIDES held another very interesting seminar on practices for financing SMEs.

In closing, I would like to point out that these meetings enable us to establish closer contact between our institution and its Governors. The discussion, so rich in its many facets and levels, strengthens the Bank's fundamental commitment. We are committed to Latin America and the Caribbean, to the different aspects of its economic and social development. These commitments are the Bank's essence. It is very important to keep our great mission in mind at all times. We are a Bank at the service of the countries, at the service of society in the broad sense; we are more than a Bank, as Felipe Herrera said. This can only be possible with an efficient organization and capable and motivated human resources. Lastly, I would like to say that we feel very closely bound by the warmth of this country and its people, for which I am sincerely grateful.

REPORT OF THE CHAIRMAN OF THE COMMITTEE OF THE IDB BOARD OF GOVERNORS ON ITS ACTIVITIES SINCE THE LAST ANNUAL MEETING

The Committee of the Board of Governors, appointed pursuant to Resolution AG-5/70, held its Eighty-seventh Meeting in Milan, Italy, on March 22, 2003. No meetings have been held since then.

I. Eighty-seventh Meeting – Milan, Italy, March 22, 2003 (document CA-452)

Summary of the Eighty-sixth Meeting of the Committee

The Committee approved the summary of its Eighty-sixth Meeting, held in Fortaleza, Brazil, on March 10, 2002 (document CA-448).

Measures for enhancing the response capacity of the Inter-American Development Bank. Progress on the implementation of the New Lending Framework (document CA-450)

At the beginning of the meeting, the Chair of the Policy and Evaluation Committee of the Board of Executive Directors read a text, included in document CA-450, by means of which the Board of Executive Directors proposed a clarification to the Committee of the Board of Governors regarding the implementation of certain aspects of paragraph 8(a) of the Annex to Resolution AG-1/02, adopted by the Board of Governors on March 1, 2002. This clarification reads as follows: “During 2003, the annual limit on the amount of Ordinary Capital policy-based lending (up to the equivalent of US$1.5 billion) may be increased by: (1) up to an additional 15 percent; and (2) the difference between the 2002 annual limit and the total amount of Ordinary Capital policy-based loans (PBLs) approved during that year. During 2004, the annual limit may be increased by: (1) up to an additional 15 percent; and (2) the difference between the equivalent of US$3 billion and the total amount of Ordinary Capital PBLs approved during 2002 and 2003. As indicated in Resolution AG-1/02, policy-based lending is subject to maintaining the aggregate lending limit of the equivalent of US$4.5 billion of Ordinary Capital resources during the 2002–2004 period, which may not be exceeded under any circumstance.”

The ensuing discussion revolved around two main issues: (i) the carryover of resources for policy-based loans (PBLs) from 2002 to 2003; and (ii) the three windows to be established under the new lending framework (emergency lending, PBLs, and investment loans).

A majority of the Governors supported the carryover of PBL resources in the context of the clarification proposed by the Board of Executive Directors and cited in paragraph 2.1 above.

With regard to the three windows, several Governors came down in favor of revising the limits and terms established for them, so that the Bank could make their use more flexible and be in a position to adopt a countercyclical role. Other Governors expressed concern over the fact that the PBLs were growing too quickly and the level of investment loans was declining. They were against reopening the discussion on the lending framework approved only one year earlier.

The Committee Chairman concluded that there was a consensus on carryover of PBL resources from 2002 to 2003, and that other matters raised during the meeting would continue to be discussed subsequently at the Special Governors’ Meeting.

Progress report on actions carried out in 2002 and proposed future actions to strengthen the Bank's development effectiveness (document CA-451)

The Executive Vice-President referred to the actions taken by the Bank in 2002 pursuant to Resolution AG-1/02, to improve the areas of: (i) country strategies and programming; (ii) project design; (iii) project implementation; and (iv) organizational and institutional matters. Mr. Flannery also referred to the actions that the Bank was planning to take in the 2003–2004 period and presented a medium-term plan of action that would be implemented to create a comprehensive development effectiveness system at the Bank.

The Governors indicated that the Bank's action in the area of development effectiveness should seek to balance results with the cost of achieving them, both from the standpoint of the Bank itself and the borrowing countries. The framework to be applied should not be costly in budget terms or staff requirements. Nor should it introduce bureaucratic processes that would impede project preparation and execution.

The Governors indicated that strengthening development effectiveness was important so that the Bank could be fully compliant with its objectives of poverty and inequality reduction as well as the Millennium Goals agreed upon in Monterrey. They noted that the Bank should make specific decisions and begin as soon as possible to implement the medium-term action plan, without waiting for all methodological aspects to be established.

Lastly, Management was asked to submit another progress report the following year on the Bank's actions to strengthen its development effectiveness. The Committee wished to see the head of the Office of Development Effectiveness appointed soon.

Other distribution:

Board of Executive Directors
Managers
Representatives

REPORT OF THE CHAIRMAN OF THE COMMITTEE OF THE IIC BOARD OF GOVERNORS ON ITS ACTIVITIES SINCE THE LAST ANNUAL MEETING

The Committee of the Board of Governors, established pursuant to Resolution CII/AG-3/92, held its Twenty-fifth Meeting in Milan, Italy, on March 22, 2003. No meetings have been held since then.

I. Twenty-fifth Meeting – Milan, Italy, March 22, 2003 (document CII/CA-88)

Summary of the Twenty-fourth Meeting of the Committee

The Committee approved the Summary of its Twenty-fourth Meeting, held in Fortaleza, Brazil, on March 9, 2002 (document CII/CA-83).

Report on the Corporation's operating and financial results for 2002. Oral presentation

The most significant aspect of the General Manager's report was that the IIC had recorded a book loss of US$41.8 million in 2002. This loss was chiefly the result of the increased provisioning necessary in those countries most affected by economic difficulties. Most of these projects involved enterprises that were having difficulties but had not gone bankrupt. The Corporation was therefore committed to helping them overcome their difficulties.

In this context, Management reduced administrative expenses, thereby achieving savings of US$1.4 million over the approved budget for 2002, downsized the Headquarters staff by 6 percent, transferred several positions to the region, and reorganized the operations structure. It also identified the following four areas of activity to help improve the Corporation's financial sustainability: (i) cost reduction; (ii) increased process efficiency; (iii) asset quality; and (iv) revenue generation.

Report by the Chairman of the IIC External Review Group (reference document CII/CS-532-1)

Mr. Pedro Pablo Kuczynski, Chairman of the IIC's External Review Group (ERG), established at the request of the Board of Governors, presented a report on the work done by the ERG to date. The ERG reached the preliminary conclusion that the future of the IIC is limited: it is very small in the context of financial flows to the Latin American private sector, it has very limited recognition in the recipient countries, it cannot afford a much needed and substantial expansion in marketing and promotion, and it suffers from some rigidities in its operation. Subject to further discussion, the ERG concluded that the revamping of the IIC should be part of an overall realignment of the IDB Group's private sector activities. The Multilateral Investment Fund (MIF) should retain the independence it was originally given under its charter, not only because of its distinct donor base, but also because of its strong track record and demonstrated performance as an agent for innovation in Latin America and the Caribbean.

The ERG is considering proposing the following organizational structure: an IDB Vice-President would be in charge of coordinating all private sector activities and would be responsible for a new affiliate that would group together the IIC and the Bank's Private Sector Department. Its capital structure would include that of IIC plus the corresponding capital within the IDB earmarked to support the private sector loans, up to 10 percent of the Bank's paid-in, callable capital and reserve resources (or alternately up to 10 percent of outstanding loans). Consequently, no new capital contributions would be required from the countries.

The Governors suggested that the ERG: (i) examine ways to promote private investment in activities for which there is a market but that the Bank does not finance; (ii) consider participating in the financing of infrastructure concessioning to private enterprises, which could take the form of guarantees or syndication; (iii) review all the legal, financial, economic, and organizational aspects that implementing the proposed arrangement would involve; (iv) consult with both IIC and IDB staff; (v) proceed with caution and be sure that the proposed objectives are achievable; (vi) determine whether it would be legally possible to transfer the capital of existing multilateral institutions with different memberships to a new entity, and examine the political and legal issues for Bank shareholders who have opted not to become shareholders of the IIC; (vii) consider the policy and supervision issues arising from the proposed new position of vice-president and its independence; and (viii) consider the proposal that the IIC be absorbed by the IDB instead of creating a new affiliate. The Governors also pointed out that before they could discuss a new structure, they would need to see an expanded strategy for IDB Group action in the private sector.

Other distribution:

Board of Executive Directors
Managers
IDB Representatives

CHAIRMAN OF THE BOARDS OF GOVERNORS
Pedro Pablo Kuczynski

PRESIDENT OF THE INTER-AMERICAN DEVELOPMENT BANK AND
CHAIRMAN OF THE BOARD OF EXECUTIVE DIRECTORS OF THE
INTER-AMERICAN INVESTMENT CORPORATION
Enrique V. Iglesias

EXECUTIVE VICE PRESIDENT OF THE BANK
Dennis E. Flannery

VICE PRESIDENT FOR PLANNING AND ADMINISTRATION OF THE BANK
Paulo Paiva

GENERAL MANAGER OF THE CORPORATION
Jacques Rogozinski

SECRETARY OF THE BANK AND THE CORPORATION
Carlos Ferdinand

INTER-AMERICAN DEVELOPMENT BANK
INTER-AMERICAN INVESTMENT CORPORATION
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Argentina

Governor

Roberto Lavagna
Ministro de Economía

Alternate Governor

Alfonso de Prat-Gay
Presidente
Banco Central de la República
Argentina

Temporary Alternate Governors

Oscar Tangelson
Viceministro de Economía y
Secretario de Política Económica
Ministerio de Economía y Producción

Guillermo Nielsen
Secretario de Finanzas
Ministerio de Economía y Producción

Gerardo Hita
Director Nacional de Proyectos con
Organismos Internacionales de Crédito
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Director Ejecutivo Suplente
Banco Interamericano de Desarrollo

Eduardo Camano
Presidente
Honorable Cámara de Diputados

Jorge Capitanich
Presidente de la Comisión de Presupuesto
y Hacienda
Senado de la Nación

Leonardo Costantino
Secretario Privado del Ministro de
Economía y Producción

Eugenio Díaz-Bonilla
Director Ejecutivo
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Pedro Lacoste
Vicepresidente
Banco Central de la República
Argentina

Leonardo Madcur
Secretario de Coordinación Técnica
Ministerio de Economía y Producción

Daniel Martin
Asesor de la Representación Financiera
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Adrian Nador
Secretario Privado del Ministro de
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Ministerio de Economía y Producción

Norberto Pagani
Gerente
Relaciones Internacionales
Banco Central de la República
Argentina

Sebastián Palla
Subsecretario de Financiamiento
Ministerio de Economía y Producción

Federico Poli
Secretario de la Pequeña y Mediana
Empresa y Desarrollo Regional
Ministerio de Economía y Producción

Armando Torres
Director de Prensa
Ministerio de Economía y Producción

Austria

Temporary Alternate Governor

Brigitte Windisch
Deputy Director
International Finance Institutions
Austrian Federal Ministry of Finance

Advisors

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Austrian Ambassador to Peru
Lima

Andreas Meindl
Commercial Counselor
Austrian Embassy in Chile
Santiago

Karla Schestauber
Senior Counselor
Office of the Executive Director
Inter-American Development Bank

Bahamas

Governor

James H. Smith, CBE
Minister of State
Ministry of Finance

Alternate Governor

Ruth Millar
Financial Secretary
Ministry of Finance

Temporary Alternate Governors

Janeen McCartney
Under-Secretary
Ministry of Finance

Ingrid Bartlett
General Manager for Groups
Ministry of Tourism

Carl Oliver
Senior Economist
Ministry of Finance

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Christopher McCoy
Chief Superintendent
Police Department

Advisors

Leslie C. Bethel
President
Notarc Management Group

Bill Coteron
Executive Director
Conference Services
Kerzner International Resorts

Joe Higgins
Director of Incentive Sales
Kerzner International Resorts

Barbados

Governor

Owen S. Arthur, MP
Prime Minister and Minister of Finance
and Economic Affairs

Alternate Governor

Grantley Smith
Director of Finance and Economic Affairs
Ministry of Economic Development

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