

00321150

GO-Meeting, Annual Proceedings

GO - 40th Meeting Board 1999-1999

Paris, France, 1999

INTER-AMERICAN DEVELOPMENT BANK INTER-AMERICAN INVESTMENT CORPORATION

PROCEEDINGS

Fortieth Annual Meeting of the
Board of Governors of the Bank

Fourteenth Annual Meeting of the
Board of Governors of the Corporation



00321150

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GO - 40th Meeting Board of 1999 -1999
Paris, France, 1999

SEC/SEC

Paris, France
March 1999

This publication contains the official record of and additional information on the Fortieth Annual Meeting of the Board of Governors of the Inter-American Development Bank and the Fourteenth Annual Meeting of the Board of Governors of the Inter-American Investment Corporation, held jointly in Paris, France, from March 15 to 17, 1999. It includes the resolutions approved between the Thirty-ninth and Fortieth Annual Meetings of the Bank and those approved during the latter of these meetings, as well as the resolutions approved between the Thirteenth and Fourteenth Annual Meetings of the Corporation and those approved during the latter of these two meetings. It also contains the addresses delivered at the meetings and the lists of participants, which include the official delegations, Senior Management and Boards of Executive Directors of the Bank and the Corporation, and observers.

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OFFICIAL RECORD OF THE MEETING

OFFICIAL RECORD OF THE MEETING

The Fortieth Annual Meeting of the Board of Governors of the Inter-American Development Bank and the Fourteenth Annual Meeting of the Board of Governors of the Inter-American Investment Corporation were held in Paris, France, from March 15 to 17, 1999.¹ The Inaugural Session was held in the Grand Auditorium of the Paris Convention Center. The plenary sessions of the Boards of Governors of the Bank and the Corporation, as well as the Seventy-ninth Meeting of the Committee of the Board of Governors of the Bank and the Nineteenth Meeting of the Committee of the Board of Governors of the Corporation, were held in the Salon Concorde, on Level 7 of the Convention Center.

The Inaugural Session opened under the chairmanship of the Governor for Colombia, Mr. Juan Camilo Restrepo Salazar. The Agendas of the meeting of the Bank and the meeting of the Corporation (see page 9) were then approved. The outgoing chairman reported on the activities of the Committee of the Board of Governors of the Bank and the Committee of the Board of Governors of the Corporation since the previous Annual Meeting² and expressed words of farewell.³

Subsequently, Mr. Dominique Strauss-Kahn, Governor for France and Minister of Economy, Finance, and Industry, was elected Chairman of the Boards of Governors. Mr. Christian Pierret, Minister of State for Industry and Temporary Alternate Governor for France, took the floor.⁴

The Inaugural Session was attended by His Excellency Mr. Eduardo Frei, President of Chile; His Excellency Mr. Jacques Chirac, President of France; and His Excellency Mr. Julio María Sanguinetti, President of Uruguay. Mr. Michel Camdessus, Managing Director of the International Monetary Fund; His Excellency Mr. César Gaviria, Secretary General of the Organization of American States; and Mr. José Antonio Ocampo, Executive Secretary of the Economic Commission for Latin America and the Caribbean, also attended the session.

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

1. Report of the Chairman of the Boards of Governors and Chairman of the Committees of the Boards of Governors on work performed since the previous Annual Meeting.

At the Inaugural Session, the Board of Governors approved the report of the Committee of the Board of Governors of the Bank and the report of the Committee of the Board of Governors of the Corporation on work performed since the previous Annual Meeting.

The report of the Committee of the Board of Governors of the Bank and the report of the Committee of the Board of Governors of the Corporation appear on pages 155 and 165, respectively.

2. The Annual Report of the Bank for 1998

During the Fifth Plenary Session, the President of the Bank reported to the Board of Governors on the activities conducted by the institution in 1998 and on the current situation of and prospects for Latin America and the Caribbean.

3. During the Fifth Plenary Session, the Governors adopted Resolutions AG-2/99, AG-3/99 and AG-4/99, approving the financial statements of the Ordinary Capital resources, the Fund for Special Operations, and the Intermediate Financing Facility account, respectively, for the fiscal year ending December 31, 1998.

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\$34.5 million in convertible currencies from the General Reserve of the Fund for Special Operations, as set forth in Resolution AG-4/99.

¹ Documents GN-2088 and CII/GN-153 contain a detailed summary of the meetings.

² Documents AB-1965 and CII/AB-639 contain the text of these reports.

³ Document AB-1974, CII/AB-645 contains the text of this address.

⁴ Document AB-2020, CII/AB-693 contains the text of the address.

4. Site and date of future annual meetings of the Boards of Governors of the Inter-American Development Bank and the Inter-American Investment Corporation

During the Fifth Plenary Session, the Board of Governors adopted Resolution AG-5/99 concerning the site and date of future annual meetings of the Boards of Governors of the Inter-American Development Bank and the Inter-American Investment Corporation, whereby appreciation was expressed for the invitations extended by the Governors for the United States, Chile, Brazil, and Italy. The Board of Executive Directors was asked, in accordance with the procedure for determining the site of the Annual Meeting appearing in Resolution AG-1/76, to submit its recommendations in due course to the Board of Governors, pursuant to the terms of reference set forth in document AB-476-2.

The Governor for Italy proposed an amendment to Section 1(a) of the Regulations of the Board of Governors, pursuant to which the annual meeting would be held in a nonregional country once every three years and in regional countries the remaining two years. The Chairman of the Board of Governors instructed the Board of Executive Directors to study this proposal and forward its recommendations to the Board of Governors for consideration.

5. Election of Executive Directors of the Bank for the 1999-2002 period

During the Closing Session, held immediately after the Fifth Plenary Session, at the request of the Chairman of the Board of Governors of the Bank, the Governors for Chile and Spain were appointed to act as tellers and were charged with supervising the balloting and tallying of the votes received in connection with the fourteenth general election of Executive Directors of the Bank. On the basis of the tellers' report, the Secretary announced that the Governors who were entitled to vote pursuant to Article VIII, Section 3(b)(ii) of the Agreement Establishing the Bank had elected the Executive Directors who were to hold office from July 1, 1999, through June 30, 2002. The following persons were elected:

Mr. Guy Lavigueur	Canada
Mr. A. Humberto Petrei	Argentina Haiti
Mr. Daniel Andrade Ribeiro de Oliveira	Brazil Suriname
Mr. Moisés A. Pineda	Dominican Republic Mexico
Mr. Jorge Baca Campodónico	Colombia Peru
Mr. Mario Marcel	Chile Ecuador
Mr. Raúl Boada	Bolivia Paraguay Uruguay
Mr. Edgard Guerra	Belize Costa Rica El Salvador Guatemala Honduras Nicaragua
Mr. George Reid	Bahamas Barbados Guyana Jamaica Trinidad and Tobago
Mr. Bruno Mangiatordi	Belgium Germany Israel Italy Netherlands Switzerland

Mr. Álvaro Rengifo Abbad

Austria
Denmark
Finland
France
Norway
Spain
Sweden

Mr. Toru Kodaki

Croatia
Japan
Portugal
Slovenia
United Kingdom

The report presented by the Secretary confirmed that, with the exception of two, all the countries had elected their respective candidates. Accordingly, and pursuant to the Regulations for the Election of Executive Directors, an extension was granted to allow those countries to elect their respective Executive Directors. The extension was not to continue beyond June 30, 1999, the date on which the current term would expire. Once the election was completed, after the two countries had voted, the respective official notification, announcing the full list of names of Executive Directors and the countries that had elected them, would be forwarded to the Board of Governors for information.

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

1. Annual Report of the Corporation for 1998

During the Fourth Plenary Session, the Governors adopted Resolution CII/AG-2/99, approving the financial statements of the Inter-American Investment Corporation for the financial year ending December 31, 1998, in accordance with Article IV, Section 2(c) of the Agreement Establishing the Corporation.

2. During the Fourth Plenary Session, the Governors took note of the introductory remarks by the Chairman of the Board of Executive Directors and of the report by the General Manager of the Inter-American Investment Corporation on its past activities and its plans for the near future.

3. Election of Executive Directors for the 1999-2002 period

During the Closing Session, held immediately after the Fifth Plenary Session, at the request of the Chairman of the Board of Governors of the Corporation, the Governors for Chile and Spain were appointed to act as tellers and were charged with supervising the balloting and tallying of the votes received in connection with the sixth general election of Executive Directors of the Corporation. On the basis of the tellers' report, the Secretary announced that the Governors who were entitled to vote pursuant to Article IV, Section 4(c) of the Agreement Establishing the Corporation had elected the Executive Directors who were to hold office from July 1, 1999, through June 30, 2002. The following persons were elected:

Mr. A. Humberto Petrei

Argentina
Haiti

Mr. Daniel Andrade Ribeiro de Oliveira

Brazil
Suriname

Mr. Moisés A. Pineda

Dominican Republic
Mexico

Mr. Enrique Camacho Matamoros

Colombia
Ecuador

Mr. Jorge Baca Campodónico

Chile
Peru

Mr. Raúl Boada

Bolivia
Paraguay
Uruguay

Mr. Edgard Guerra

Costa Rica
El Salvador
Guatemala
Honduras
Nicaragua

Mr. George Reid

Bahamas
Barbados
Guyana
Jamaica
Trinidad and Tobago

Mr. Georges Cahuzac

France
Germany
Switzerland

Mr. Rits De Boer

Austria
Denmark
Italy
Netherlands

Mr. Álvaro Rengifo Abbad

Israel
Japan
Spain

The report presented by the Secretary confirmed that, with the exception of two, all the countries had elected their respective candidates. Accordingly, and pursuant to the Regulations for the Election of Executive Directors, an extension was granted to allow those countries to elect their respective Executive Directors. The extension was not to continue beyond June 30, 1999, the date on which the current term would expire. Once the election was completed, after the two countries had voted, the respective official notification, announcing the full list of names of Executive Directors and the countries that had elected them, would be forwarded to the Board of Governors for information.

Carlos Ferdinand
Secretary of the Bank and of the Corporation

AGENDAS



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

1. Election of the Chairman of the Board of Governors
2. Report of the Committee of the Board of Governors on the work done since the last annual meeting
3. Annual Report of the Bank. Financial statements for 1998:
 - Ordinary capital resources
 - Fund for Special Operations
 - Intermediate Financing Facility Account
4. Election of Executive Directors for the term 1999 to 2002
5. Place and date of future annual meetings of the Boards of Governors of the Inter-American Development Bank and the Inter-American Investment Corporation

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

1. Election of the Chairman of the Board of Governors
2. Report of the Committee of the Board of Governors on its work since the last annual meeting
3. Annual Report of the Corporation. Financial statements for 1998
4. Remarks by the Chairman of the Board of Executive Directors
5. Election of Executive Directors for the term 1999 to 2002

RESOLUTIONS

**RESOLUTIONS ADOPTED BETWEEN THE THIRTY-NINTH AND
THE FORTIETH ANNUAL MEETINGS OF THE BANK**

RESOLUTION AG-6/98

REMUNERATION OF EXECUTIVE DIRECTORS

WHEREAS:

The Committee of Governors designated pursuant to Resolution AG-8/91 has examined the situation with respect to the remuneration of the Executive Directors and made recommendations in that regard;

The Board of Governors

RESOLVES:

To accept the recommendation of the Committee and, pursuant to Article VIII, Section 2(b)(v), of the Agreement Establishing the Bank, to increase by 3.5 percent the remuneration paid to the Executive Directors, effective April 1, 1998.

(Adopted July 29, 1998)

RESOLUTION AG-7/98

AUTHORIZATION TO GRANT THE BOARD OF EXECUTIVE DIRECTORS
INCREASED FLEXIBILITY TO APPROVE EMERGENCY SECTOR LOANS

WHEREAS,

The economies of many of the Bank's borrowers have been negatively impacted by recent developments in the international financial markets, and the Bank wishes to make emergency loans to assist its borrowers in mitigating these impacts;

The Board of Governors has, in approving Document AB-1704, limited (1) the amount of policy based lending to 15% of the cumulative lending program under the Eighth Replenishment; (2) the amount of lending to A and B countries to 65% of total lending; and (3) the percentage of total costs of any investment project that may be financed in foreign exchange by the Bank; and

The limits on the amount of policy based lending, the amount of lending to A and B countries and the percentage of costs financed in foreign exchange create a severe constraint on the Bank's ability to assist its borrowing members with emergency loans; and the Directors and management of the Bank have concluded that the limits established in Document AB-1704 must be relaxed temporarily if the Bank is to participate in concerted international efforts to support its borrowers.

The Board of Governors

RESOLVES:

(1) That, for a period of one year from the date of this resolution, the Board of Executive Directors is authorized to approve emergency loans as exceptions to (a) the 15% cap imposed on the amount of total resources allocated to policy based lending in accordance with paragraph 2.55 of Document AB-1704; (b) the indicative goal to lend 35% of total lending to Group C and D countries in accordance with paragraph 4.5 of Document AB-1704; and (c) the limits on the percentage of total costs of any investment project which may be financed in foreign exchange by the Bank as set forth in paragraph 2.91 of Document AB-1704; and

(2) That the Board of Executive Directors shall determine which loans shall be considered "emergency loans" to be included within the exception established in paragraph 1 of this resolution.

(Adopted December 11, 1998)

RESOLUTION AG-1/99

AGREEMENT ON CONCESSIONAL RESOURCES
OF THE BANK AND RELATED MATTERS

Whereas, the Inter-American Development Bank (the "Bank") needs additional convertible currency concessional resources to (1) carry out its mandate of poverty reduction, especially in the poorest countries; and (2) meet the exceptional needs caused by recent natural disasters;

Whereas, the Bank has substantial local currency resources in the Fund for Special Operations which, if converted, would provide additional resources to help the Bank fulfill its mandate in the poorest countries and deal with the natural disasters in some of these countries; and

Whereas, the Committee of the Board of Governors met on December 9, 1998, discussed the contents of Document CS-3170-14 entitled "Meeting the Need for Concessional Resources", agreed on a proposed ten point program for concessional resources and related matters, and recommended that this agreement be submitted to the full Board of Governors for approval;

The Board of Governors

RESOLVES THAT:

The agreement recommended by the Committee of the Board of Governors which is set forth in Annex A to this resolution is hereby approved.

The Board of Executive Directors and the Management are hereby directed and authorized to take all necessary steps to implement the agreement set forth in Annex A.

(Adopted February 22, 1999)

Annex A

Agreement reached at the Seventy-eighth Meeting of the
Committee of the Board of Governors
(December 9, 1998)

Brazil makes available 80% (US\$718 million) of local currency. All other countries except for D-2 countries make available 65% (US\$1,435 million) of local currency.

Taking into account availability, types and sources of resources, and the agreed lending program, conversion flows will be established by the Board of Executive Directors in consultation with Management.

Total D-2 country resources will be converted after the year 2009. In the exceptional event that the D-2 countries are not able to fulfill this commitment, non-borrowing countries will undertake to find a solution to the problem without further commitment by borrowing countries.

Each non-borrowing country will make its best efforts to accelerate payment of its flow of FSO convertible-currency resources under the Eighth General Increase in Resources.

The agreement implies acceptance by the Board of Governors that the net income of the Bank's Ordinary Capital, beyond that provided for in the Eighth Replenishment agreement, will not be allocated to the FSO or HIPC.

The remaining local-currency resources will be available to the issuing countries in accordance with the applicable regulations.

The non-borrowing countries undertake to make their best efforts in contributing to the Fund for Reconstruction of Central America, on a voluntary basis.

The IDB contribution to the HIPC facility for Honduras, if eligible, will be financed from FSO resources.

The proposals in document CS-3170-14 regarding "Improving the Bank's capacity for effective management", "Country distribution of lending", and "Lending to the private sector" are agreed.

The IFF, FSO, and TC financial program, and HIPC for Nicaragua, as proposed for the years 2000-2008, and the US\$100 million contribution to finance reconstruction for Central America, as set forth in document CS-3170-14, are agreed.

**RESOLUTIONS ADOPTED AT THE FORTIETH
ANNUAL MEETING OF THE BANK**

RESOLUTION AG-2/99

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, 1998, containing the general balance sheet and the statement of profit and loss, are approved.

(Adopted March 17, 1999)

RESOLUTION AG-3/99

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, 1998, 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 of the equivalent of US\$34,500,000 in convertible currencies of the General Reserve of the Fund for Special Operations.

(Adopted March 17, 1999)

RESOLUTION AG-4/99

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, 1998, containing the general balance sheet and the statement of changes in fund balance, are approved.

(Adopted March 17, 1999)

RESOLUTION AG-5/99

PLACE AND DATE OF FUTURE ANNUAL MEETINGS OF THE
BOARDS OF GOVERNORS OF THE INTER-AMERICAN DEVELOPMENT BANK
AND THE INTER-AMERICAN INVESTMENT CORPORATION

WHEREAS:

The Governors for the United States, Chile, Brazil, and Italy have, prior to the Fortieth Annual Meeting of the Board of Governors, offered their countries as sites for annual meetings of the Boards of Governors of the Bank and the Corporation to be held in 2000 and subsequent years; and

It is expected that during the Fortieth Annual Meeting of the Bank's Board of Governors other Governors will offer their countries as the sites of future annual meetings of the Boards of Governors of the Bank and the Corporation;

The Board of Governors

RESOLVES:

1. To express its appreciation for the invitations extended by the Governors for the United States, Chile, Brazil, and Italy, as well as such other invitations as may be extended during the course of the Fortieth Annual Meeting of the Board of Governors.

2. To instruct the Board of Executive Directors, following the procedure approved pursuant to Resolution AG-1/76, to present its recommendations concerning the place and date 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 17, 1999)

**RESOLUTIONS ADOPTED BETWEEN THE THIRTEENTH AND THE
FOURTEENTH ANNUAL MEETINGS OF THE CORPORATION**

RESOLUTION IIC/AG-3/98

DESIGNATION OF EXTERNAL AUDITORS

The Board of Governors

RESOLVES:

That, pursuant to Article IV, Section 2(c)(vii), of the Agreement Establishing the Inter-American Investment Corporation and in accordance with Resolution CII/DE-5/95 adopted on February 21, 1995, the firm of Price Waterhouse is selected, with respect to the fiscal year 1998, to serve as external auditors to examine the general balance sheets and the statements of profit and loss of the Institution, in accordance with Section 8 of the By-laws.

(Adopted August 3, 1998)

RESOLUTION IIC/AG-1/99

ADMISSION OF BELIZE TO MEMBERSHIP IN THE CORPORATION
AND SPECIAL CAPITAL INCREASE

WHEREAS, Article II, Section 1(b) of the Agreement Establishing the Corporation (the "Agreement") provides that the Inter-American Development Bank (the "IDB") member countries that are not founding members of the Corporation may accede to the Agreement and become members of the Corporation on such date and in accordance with such conditions as the Board of Governors of the Corporation may determine by a majority of at least two-thirds of the votes of the members, which shall include two-thirds of the Governors;

WHEREAS, Article II, Section 2(c)(i) of the Agreement provides that the Board of Governors may increase the authorized capital stock of the Corporation by two-thirds of the votes of the members, when such increase is necessary for the purpose of issuing shares, at the time of initial subscription, to members of the IDB other than founding members, provided that the aggregate of any increases authorized does not exceed 2,000 shares;

WHEREAS, Belize, a member country of the IDB, has applied for admission to membership in the Corporation; and

WHEREAS, pursuant to Section 9 of the By-laws of the Corporation, and after consultation with representatives of the Government of Belize, the Board of Executive Directors of the Corporation hereby recommends to the Board of Governors to admit Belize as a member of the Corporation pursuant to the application by them submitted.

The Board of Governors

RESOLVES:

1. That Belize shall become a member of the Corporation when the Chairman of the Board of Executive Directors of the Corporation shall have declared that Belize has fulfilled all the following requirements:
 - (a) It shall have subscribed to 30 shares of the capital stock of the Corporation having a par value of US\$10,000 (ten thousand United States dollars) per share, on the following basis:

The amount subscribed to the capital stock of the Corporation shall be subject to payment made in United States dollars in four equal yearly installments within four years after the date on which Belize accedes to the Agreement, or by such future date as the Board of Executive Directors may determine.
 - (b) Its duly authorized representative shall have signed the original of the Agreement deposited with the General Secretariat of the IDB.
 - (c) It shall have deposited with the General Secretariat of the IDB an instrument setting forth that it has accepted or ratified, in accordance with its laws, the Agreement and all the terms and conditions prescribed in this Resolution, and that it has taken the steps necessary to enable it to fulfill all of its obligations under the Agreement and this Resolution.

- (d) It shall have represented to the Corporation that it has taken all action necessary to sign the Agreement and deposited the instrument of acceptance or ratification as contemplated by Section 1(b) and 1(c) of this Resolution and it shall have furnished to the Corporation such information in respect of such action as the Corporation may have requested.
- 2. Belize may accept the conditions and fulfill the requirements established for membership until January 18, 1999, provided, however, that if extraordinary circumstances are deemed by the Board of Executive Directors so to warrant, the Board may postpone such date.
- 3. Pursuant to Article II, Section 2(c)(i) of the Agreement, in order to effect this recommendation, the Corporation's authorized capital stock is increased in the amount of US\$300,000 (three hundred thousand United States dollars) through the issuance of 30 shares in favor of Belize, in accordance with the terms and conditions prescribed in this Resolution.

(Adopted January 20, 1999)

**RESOLUTION ADOPTED AT THE FOURTEENTH
ANNUAL MEETING OF THE CORPORATION**

RESOLUTION IIC/AG-2/99

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 certified that the balance sheet and the statements of income and retained earnings and of cash flow were prepared in accordance with generally accepted accounting principles;

The Board of Governors

RESOLVES:

That the financial statements of the Corporation with respect to the fiscal year ended December 31, 1998, containing the balance sheet and the statements of income and retained earnings and of cash flow, are approved.

(Adopted March 16, 1999)

SCHEDULE OF SESSIONS

SCHEDULE OF SESSIONS

Wednesday, March 10

9:00 a.m. to 6:30 p.m. Registration of participants

Thursday, March 11

8:00 a.m. to 6:30 p.m. Registration of participants

9:30 a.m. to 7:00 p.m. Forum: Development and Culture

Friday, March 12

8:00 a.m. to 6:30 p.m. Registration of participants

9:30 a.m. to 6:00 p.m. Forum: Development and Culture (cont.)

Saturday, March 13

8:00 a.m. to 6:30 p.m. Registration of participants

9:00 a.m. to 1:00 p.m. Seminar: Powerful Alliance: SMEs, Technology, and Private Capital

9:30 a.m. to 5:45 p.m. Seminar: Facing up to Inequality

3:30 p.m. Preliminary Session of Heads of Delegation to the Fourteenth Annual Meeting of the Board of Governors of the Corporation; followed by Meeting of the Committee of the Board of Governors of the Corporation

Sunday, March 14

8:00 a.m. to 6:30 p.m. Registration of participants

9:00 a.m. to 1:00 p.m. Seminar: New Initiatives to Tackle International Turmoil

2:30 p.m. to 6:30 p.m. Seminar: Breaking the Poverty Cycle: Investing in Early Childhood

3:30 p.m. Preliminary Session of Heads of Delegation to the Fortieth Annual Meeting of the Board of Governors of the Bank; followed by Meeting of the Committee of the Board of Governors of the Bank

Monday, March 15

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 16

9:00 a.m. to 5:30 p.m. Seminar: The Euro and its International Impact

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

3:00 p.m. Fourth Plenary Session (Inter-American Investment Corporation)

Wednesday, March 17

9:30 a.m. to 12:45 p.m. Fifth Plenary Session and Closing Session

ADDRESSES

ADDRESSES

FIRST PLENARY SESSION

MARCH 15, 1999

INAUGURAL SESSION

MR. JUAN CAMILO RESTREPO SALAZAR, OUTGOING CHAIRMAN OF THE BOARDS OF GOVERNORS OF THE INTER-AMERICAN DEVELOPMENT BANK AND THE INTER-AMERICAN INVESTMENT CORPORATION AND GOVERNOR FOR COLOMBIA, AT THE INAUGURAL SESSION

The Inter-American Development Bank has brought us to this city where, as Victor Hugo so rightly said, ideas are developed to be enjoyed and put into practice elsewhere. We have come to once again fulfill our commitment to dialogue and multilateral cooperation, and to reaffirm our determination to continue the process of transforming Latin America and the Caribbean.

Liberty, equality, fraternity have always been guiding principles for the Americas. Nevertheless, I think that until now we have practiced liberty more than equality or fraternity in Latin America. We hope that this meeting of the Boards of Governors will help us find a balance.

On behalf of the member countries, we should like to express our deep appreciation to the Parisian authorities and to all of France for their hospitality and their efforts, which have made the smooth progress of this meeting possible.

Colombia has had the honor of chairing the Boards of Governors of the Inter-American Development Bank and the Inter-American Investment Corporation in the year in which the Bank celebrated the fortieth anniversary of the OAS resolution that provided for its establishment.

In 1998, with operations totaling close to US\$10 billion, the Bank showed that it was capable of responding effectively to the region's needs and that it is an essential partner in the financing of economic and social development programs in its borrowing member countries.

Colombia was especially pleased to have been able to help resolve the problem of scarce concessional resources at the IDB. Despite the exchange and fiscal difficulties being experienced by some of the borrowing member countries, the commitments they have made to forgo the use of a significant percentage of the local currencies available in the Fund for Special Operations constitute an act of generosity towards the 12 countries who receive concessional loans, and in particular Bolivia, Nicaragua, Haiti, Honduras, and Suriname.

Indeed, an additional US\$2.4 billion were channeled through this agreement to the countries most in need. There are still some gaps to fill with regard to the possibility of a debt alleviation program for Honduras and the financing of country and regional technical-cooperation operations in all the borrowing member countries. We hope that the nonborrowing countries will do everything they can to strengthen the FSO and to cover its deficiencies, advancing the contributions to which they committed during the Eight Replenishment negotiations.

The Latin America of today is very different from the Latin America of 40 years ago. Our countries have made enormous progress in terms of demographic and health indicators. They have urbanized vigorously and have advanced significantly in their industrialization and export-diversification processes. They have triumphed in the fight against illiteracy, in the expansion of essential public services, and in providing opportunities to the middle-classes.

In addition, with the experience gathered regionally and together with a new generation of economists and institutions that shaped what was called the "Washington consensus", Latin America discovered the markets, opened its borders, and entered a period of far-reaching economic and political reforms.

Today it is clear that this Washington consensus needs to be rethought in at least three areas. The first and most strongly felt by many Latin American countries refers to the need to evaluate the impact of market globalization. The second calls for deepening the relationship between monetary and exchange policies. Lastly, the need for rapid response on the part of multilateral organizations to face the increased volatility of international markets has become obvious.

In recent years, the values of democracy have become firmly instilled in our region. We have been able to maintain macroeconomic discipline, defeat hyperinflation, and make public services more efficient. Yet this has not been enough. As the IDB noted in a recent study on the impact of the reforms, in the 1990s not only did we grow on average at rates below those that characterized the 1960s and 1970s, but unemployment in many of our countries is reaching explosive levels.

In terms of income distribution, progress has been neither substantial nor generalized. Today, there are still 150 million people living in poverty in the region. We must give new meaning to the role of the State in each of our modern societies.

In the proposal on guidelines for future Bank action, submitted to us for consideration last year, the need for social reforms in tandem with economic reforms was brought to our attention.

We can no longer delay placing an emphasis on building States where the rule of law prevails, in which the core of any legal or economic institution is the human being and his or her dignity as such. We are confident that in Latin America it is possible to create room for the coexistence of a strong private sector, a dynamic and competitive economy, and a strengthened State that works efficiently toward advancing social justice.

For Colombia, strengthening the State must necessarily proceed along the paths of peace. To that end, from the outset the government of President Pastrana has made it clear that ending the long period of violence that the country has experienced must be a

national priority. We know that, without the scourges of guerrilla activity, the paramilitary, and drug trafficking, our economy could have grown by an additional two percent annually.

As a significant first step toward peace, the national government has offered all the guarantees and conditions needed to establish a favorable atmosphere that promotes rapprochement between the parties in conflict. Moreover, the Solidarity Fund for Peace has been established as an instrument for channeling resources, and for coordinating action at the institutional, national, international, regional, and local levels. The Fund has three sources of financing: contributions from the national budget; proceeds from peace bonds that will be purchased by Colombian companies and citizens with substantial incomes; and lastly, international cooperation, which will allow resources from all countries and multilateral credits to be mobilized to promote peace. The establishment of the Solidarity Fund for Peace is a real opportunity for the international community to contribute effectively to the settlement of armed conflict in Colombia. A generous contribution to the Peace Fund will reinforce our efforts toward achieving this goal, in which the IDB, under the leadership of its President, has played a fundamental role.

Adjustment of public finances was an equally important task for the new government. All necessary measures have already been implemented for 1999. Spending was cut by one percent of GDP. A tax reform was approved that will generate revenue equal to approximately one percent of GDP, and the Congress has granted the government the authority to streamline the public sector. In this context, the IDB approved a US\$500 million credit for deepening structural reforms in the country.

In order to avoid a systemic crisis in the financial sector, a temporary tax on financial transactions was passed in order to obtain resources to strengthen the financial sector without incurring quasi-fiscal costs. All of this helped to provide access to external borrowings, and Colombia has now obtained virtually all the financing it needs for the remainder of this year.

At the outset of the current administration, the exchange band moved nine points, foreshadowing the shift that would take place in December. This movement calmed the exchange market and ended to expectations of devaluation, making possible a 40 percent cut in interest rates in the last six months.

This past January 25, in the midst of this reorganization process, our country was struck by a terrible earthquake that destroyed most of what we call "the coffee belt". All Colombia was moved by the outpouring of generosity from the international community. I should like to take this opportunity to thank all countries and the Inter-American Development Bank for their solidarity. Thanks to the new emergency lending facility established by the IDB late last year to support countries faced with natural disasters, we were able to receive, very expeditiously, the first disbursements of a US\$20 million loan. The costs of the investments we must make in order to recover are very great. The estimated cost for rebuilding the affected area is approximately one percent of GDP.

The reasons that motivated us to create the Inter-American Development Bank forty years ago take on special significance today. We are living in a world that is becoming increasingly complex, in which political, economic, and technological events are moving at a dizzying pace and are extending beyond the old geographical and political borders. Old ideas of sovereignty have had to give way to the rules of integration and multilateral cooperation. The years 1998 and 1999 were complicated for Latin America and the Caribbean. The uncontrollable forces of nature as well as movements in the international financial markets that originated elsewhere pummeled our economies.

As the IDB's Office of the Chief Economist put it so well, at the outset of the crisis in August 1998 most of the world's emerging markets, including those in our region, lost a great deal of their access to external financing even though their economies do not show any significant intrinsic weaknesses. What is even worse, the markets seemed to make no distinctions. Financial volatility and increases in spreads for Latin American bonds were the result of the contagion effect. Investors rushed to cover their positions and to pull out investments in emerging markets in light of the uncertainty created by the Russian moratorium.

We are aware that our countries must come to depend less and less on the fluctuations of external financing by increasing their internal savings capacity and reducing their fiscal deficits.

If we make strides with respect to the variables outlined above, we will be able to hold firm in our insistence that the international community open its markets to us. We need to promote greater trade flows in such protected sectors as agriculture. In this sphere, we need to do more. What better setting than this meeting of the Governors in Paris, taking inspiration from the European Union's proven capacity for dialogue, to issue a call along these lines to the economic ministers and heads of government of the Group of Seven nations.

In addition, we should like to encourage the International Monetary Fund, the World Bank, and the other multilateral financial organizations here with us today to strengthen the instruments at their disposition to help countries overcome their crises.

Happily, the Board of Governors of the Inter-American Development Bank decided to establish a new emergency lending facility that has enabled us to have access to additional resources in a timely and expedited manner, subject to achieving clear reform goals.

It is a source of particular satisfaction for Colombia to have presided over the meetings of the Committee of the Board of Governors that led to a more judicious indicative target for distribution of the volume of lending among the various countries.

To that end, it was arranged that 35 percent of the Bank's lending must be directed to countries with a per capita gross domestic product below US\$3,200. This indicator is much better suited to gauge the IDB's efforts in the countries in most need in the region. The private sector window has also been strengthened. Thus the Bank will be able to channel a greater volume of resources to

businesses that are entering into competition in the public utilities. Similarly, we applaud the authorization given for an increase in the maximum value and percentages for financing projects in Group C and D countries. Without doubt, these actions will have a positive impact on private-sector businesses in Latin America and the Caribbean.

The commitment of the member countries of the Inter-American Investment Corporation to increase the institution's capital by US\$500 million marks a major step forward in supporting small and medium-sized enterprise. Through this increase, their access to scarce external financing is improved, as are conditions for creating new job opportunities.

The support that we received from all the member countries during this year was fundamental for reaching these agreements, and provides further proof of their confidence in the future of the region and in the opportunities that multilateral cooperation affords.

We should like to express our deep gratitude to all the members, and most especially to the President of the Bank, Mr. Enrique V. Iglesias, who has made development in Latin America and the Caribbean a vital mission.

First of all, I would like to thank my fellow Governors of the Bank for having asked France to chair our annual meeting. The Governor for France, Mr. Dominique Strauss-Kahn, has unfortunately been called to Brussels today to attend the Council of Ministers of Finance of the European Union, which is to examine the multiyear public finance plan. The countries that have adopted the euro as their currency are supposed to perform a joint review of the budgetary policy of each country, and today it is France's turn to present its program to its partners. At a time when the euro represents an essential enclave of stability for an international financial community that is experiencing turbulence elsewhere, I am sure you will understand that Mr. Strauss-Kahn himself had to represent France in Brussels. He therefore asked me to chair this meeting on his behalf. I can assure you that he is of course anxious to return this very evening and to join you for the rest of this event here in Paris.

It is a great honor for France and for me to host this meeting in Paris. This is an important time for our Bank. For one thing, the IDB is celebrating forty years of development work in Latin America and the Caribbean, an anniversary that also falls at an important time when world attention is focusing on the stakes of development and development financing in the region.

In recent months Latin America has been suffering from the impact of the international financial crisis that has been sweeping the world.

Despite a decade of very rapid growth and development, the Hemisphere must face international financial instability. Private capital, which in a few years has become the primary source of financing for emerging countries, is being diverted to less risky investments. At the same time, plunging growth in Asia led to a drop in the prices of raw materials, which are also an essential source of income for developing and emerging countries.

In this context, restoring stability and growth should naturally be our priority, while we continue to target long-term development. Our Bank, our individual countries, and the entire international financial system should work towards this goal together.

I would like to discuss three points in particular that I believe should guide the activities of the Inter-American Development Bank and that reflect the keen spirit of cooperation among our countries that the Bank embodies: the reforms needed to overcome the crisis, private-sector development, and the sense of solidarity that binds us in the Bank.

Ambitious reforms are needed to overcome the crisis and pursue development

The Bank has already adapted its rules for intervention so that it can provide support, alongside the International Monetary Fund and the World Bank, for the countries in crisis. The IDB's support for early intervention in crisis situations is essential and fully consistent with its mandate. This expression of solidarity is in no way incompatible with the Bank's long-term mission to provide financing for development. On the contrary, the Bank must not allow its valiant, longstanding efforts to be jeopardized by economic shocks.

While the Bank has done fine work for all its borrowing members, for certain countries to achieve recovery, reforms clearly must be implemented, especially in the financial sector. On a larger scale, we need a worldwide effort to organize our own monetary and financial system and oversight of capital flows.

We must strengthen the capacity of international financial institutions to oversee capital flows and prevent disequilibria from occurring. We must also establish common rules to fight financial transfers that are not transparent, particularly those conducted through offshore centers. This approach has become clearly necessary since the beginning of the Asian crisis. Some progress has been made in certain institutions, but we have to go further.

We must also strengthen the governance of our institutions to give them the mandate and the political legitimacy necessary to intervene on behalf of their Governors during a crisis situation. To this end, France has proposed that the Interim Committee of the International Monetary Fund be strengthened by transforming it into a ministry-level decision-making body, the Council established under the IMF Charter. Such a body, on which all the member countries are represented, is the most appropriate for making policy decisions on financial stability and crisis management that concern the entire international financial community.

Similarly, the governing bodies of development banks need to be strengthened to help them better support the borrowing countries. In this spirit, IMF President James Wolfensohn has proposed enhancing the role and status of the Development Committee. France fully supports this approach.

Today, the primary lender and provider of assistance for Latin America is the Inter-American Development Bank. It is therefore only natural that at the political level as well, IDB President Enrique Iglesias should have an opportunity to see us renew our confidence in his action and hear our suggestions, on a regular basis. I would therefore like to propose that we meet at least once a year in a ministry-level Committee of Governors that would be called the Latin American Development Committee.

The IDB and the Inter-American Investment Corporation have a major role to play in private-sector development

Private investment is the engine of financing for development in emerging countries.

At a time when investors may turn away from emerging countries, the IDB and the IIC have a major role to play in helping restore investor confidence.

The purpose of the decision by the Board of Governors of the Bank to increase the volume of private-sector operations and to augment the IIC's capital is to give the Bank Group the means to take decisive, effective action to promote investment. France fully supports these decisions, and is pleased with the admission of new members to the Corporation, testimony to its successful support for small and medium-sized enterprises, which represent an essential link in the economy, and in development.

I hope that the Bank Group continues energetically and effectively in this direction.

However, it is important to properly target efforts to promote private investment. Like other international institutions that work to develop the private sector, the Bank and the Corporation should not focus on quantity. Regardless of the type of operation or its size, the Bank and the Corporation have a volume of operations that remains small compared with overall flows. Alone, they therefore cannot remedy a massive outflow of private capital. Only action by the countries concerned and the international community as a whole can do that. Moreover, higher volumes could jeopardize the quality of their operations.

Accordingly, the Bank and the Corporation must seek two essential effects to restore investor confidence:

- (i) a demonstration effect, through the quality of their operations; and
- (ii) a leveraging effect, by attracting private financing.

Lastly, we must beware of facile solutions, which have a primarily quantitative approach and would lead to long-term problems without even providing substantial improvements in the short term. An example of such risky instruments is guarantees for bond issues. It is important not to eventually create a debt structure problem in the borrowing countries. Care must be taken instead to create a genuine leveraging effect and ensure that it would be greater than that of lending. A crowding-out effect must be avoided at all costs. Guarantees can be a useful, effective instrument to promote investment, provided they remain in the framework of a specific investment or financing project. We should therefore be prudent in our use of this instrument, and I hope that more in-depth studies can be conducted on the leveraging effect and systemic risk before guarantee operations are launched.

I would like to commend the President of the Bank for his decisive efforts to give the Bank Group the necessary technical and financial capacity to handle the issues at stake. France is fully confident that the Bank will meet this objective.

The Bank's members are bound by a sense of solidarity towards Latin America and the Caribbean

In 1998, the Bank affirmed its role as a pioneering institution for development financing in Latin America and the Caribbean. Spurred by the President, the community of the Bank's member countries was able to mobilize the entire international community to help finance reconstruction of the Central American countries devastated by Hurricane Mitch.

At the same time, the borrowing countries of the Bank demonstrated a tremendous sense of regional solidarity by reaching a long-awaited agreement with all the member countries on the Bank's concessional resources.

In my opinion, these two major achievements reflect the solid ties of solidarity among our countries embodied by the Bank. The effort made by the borrowing countries for the concessional resources of the Bank will mobilize enough internal Bank resources to finance a substantial development program for the poorest countries. Concurrently, the nonborrowing countries are directly mobilizing financial resources for the poorest countries, which urgently need them, especially for reconstruction in Central America.

France expressed this sense of solidarity by providing immediate aid to the countries affected by Hurricane Mitch, by writing off its official debt with those countries. France has also provided financial assistance for the plan to support countries in crisis.

The Bank has been the hub of these expressions of solidarity and I know that President Iglesias has a great deal to do with it.

France itself has made a commitment to this effort by maintaining the highest level of official aid for development among the G7 countries. The European Union as a whole is the primary source of official aid to all the regions in the world. In Latin America, it accounts for 42% of the total.

Since this aid is essential for the poorest countries, both France and Europe wish to maintain it at a high level. In particular, France would like to see a special effort being made for the heavily indebted poor countries as the second millennium closes. It has therefore proposed an initiative to its partners to forgive the debt burden for these countries for a generation.

France is proposing that, once a country is deemed eligible for the Heavily Indebted Poor Countries Initiative, its commercial debt be reduced to the level required to achieve sustainability, beyond 80% if necessary. It is also proposing that the burden of official concessional debt be canceled for 30 years, and that all of this support be provided upon eligibility.

We should also bear in mind that other countries suffer from an excessive debt burden. France has therefore proposed that all countries eligible under Naples terms have two thirds of their commercial debt canceled instead of just 50%. We will have to take a position on this matter in the Paris Club very soon. We can also help indebted countries reduce the service on their debt and attract private capital through debt-for-investment swaps. France unconditionally supports this approach.

All of France's efforts are meaningless, though, if they are not shared by all the creditors. France therefore stresses the need for equitable sharing of official development financing. I hope that the multilateral institutions and donor countries can make contributions proportionate to France.

In conclusion, I would like our meeting to take place under the sign of confidence in our Bank, its staff, and its leaders, and in the vigor and relevance of its action.

I hope that the meeting will enable us to provide optimal momentum and guidance for the action of the Inter-American Development Bank and the Inter-American Investment Corporation. On behalf of France, I intend to do my best to serve this objective while chairing this annual meeting.

STATEMENT 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,
AT THE INAUGURAL SESSION

Introduction

I should like, first of all, to extend a very warm welcome to the Governors of the Inter-American Development Bank and Inter-American Investment Corporation, and the many other colleagues and friends who are joining us for this Annual Meeting of the Boards of Governors.

We wish to offer a very special vote of thanks to the Government of France and to its Finance Minister, Mr. Strauss-Kahn, for their support in staging this year's annual meeting and their assistance with the many arrangements that have set the scene for our gathering in these splendid surroundings.

Visiting Paris has always been a delight, indeed a privilege, for people the world over, but this city holds very special meaning for the people of Latin America and the Caribbean. Our countries and our history owe much to France and its legacy to the culture and values that are the cornerstones of our Western civilization.

Our affinity, our sense of communion and spiritual identity with France, have been distilled in the words of the French poet of Uruguayan origin, Jules Supervielle, who wrote:

*Far off within ourselves
We hold France in our arms
Each thinking himself unseen
And alone with her.*

It is particularly gratifying to be assembled in Paris this year as the Inter-American Development Bank marks forty years of partnership with the region. The birth of the Bank four decades ago gave tangible form to a shared vision of the governments of Latin America, the Caribbean, and the United States. Its creation was, for its time, a brave adventure driven by a bold mission: to fashion an institution that would serve the region's economic and social interests, one that would be creative but rest on firm footings, imprinting its own unique style on its relations with its member governments and with Latin American and Caribbean society.

Some twenty-five years ago the Bank broadened its horizon to welcome countries from outside the region as full members. France was one of the first nonregional partners in our mission to further the economic and social advancement of Latin American and Caribbean nations individually and as a region.

It fell to the Bank's first president, Felipe Herrera, to begin shaping our organization's personality. His successor, Antonio Ortiz Mena, and I in turn have sought to preserve and fortify the traits that make us unique. Chief among them are our commitment to keep pace with the forces of change, as nations forge truly modern economies; to search for solutions to the region's multifaceted social problems; and to help propel regional integration as the backbone of Latin American and Caribbean economic life today. In so doing we have held fast to our own unique approach. Against that backdrop, the regional member countries, which hold a majority of the Bank's capital and play a significant role in directing and managing the institution, have demonstrated at every turn their commitment to responsible action. Today, the Bank's capital stock stands at US\$100 billion. Our institution has mapped out a set of ambitious goals for itself, not least among them the Eighth Replenishment targets, and in their pursuit it is deploying dynamic new instruments in a continuing quest to improve efficiency within its own walls. Thus newly strengthened, the Bank will continue to serve Latin America and the Caribbean in a timely and effective manner.

I shall take the opportunity here to extend special thanks to the President of Brazil, Mr. Fernando Henrique Cardoso, for the invitation to hold a meeting at the end of this year in Quitandinha, Petrópolis, to mark the Bank's fortieth anniversary and provide us with a forum in which to think about the future course of our institution. It was in that very city, in 1954, that the idea of creating a development bank was given fresh impetus and, thanks to the impressive efforts of President Juscelino Kubitschek in the following years, the Bank was formally established in 1959. The Quitandinha meeting will give us a chance to reflect on what we have accomplished thus far, and on the role that will fall to the Bank in Latin America and the Caribbean in the coming decades.

As far as 1998 is concerned, the Bank remained the region's main source of development resources for the fifth consecutive year. Both disbursements and approvals were at record levels of US\$6.6 billion and US\$10 billion, respectively. The Corporation approved US\$223 million, over half of these resources having gone to support projects in the smaller countries. Multilateral Investment Fund approvals totaled US\$137 million. The details are contained in the annual reports for the Bank and the Corporation, which have been distributed to the Governors.

I shall now turn to events and trends in the global economy that have implications for Latin American and Caribbean development, and share some of the lessons learned from the economic events of 1998 and the region's performance this past year.

International Economic Trends

It is not my intention here to offer an in-depth account of the global economy in the recent past; all of you are fully versed in the events of these last twelve months. I could perhaps sum up 1998 as a year of sharp contrasts that have left an indelible mark on the emerging economies, the Latin American and Caribbean economies among them.

Although the performance of the major industrial economies in 1998 was sufficiently strong to sustain two percent growth overall in gross domestic product, there is much debate today as to the prospects for those economies in the immediate future. Many analysts see them as solidly positioned for continuing growth; others are not so sure. The doubters point to concerns and uncertainty about the likelihood that the growth rates of recent years can realistically be sustained. We feel confident, however, that the industrial economies overall, and the U.S. economy in particular, will continue to grow, and that the global growth rate will hold firm in 1999.

The situation has been less rosy for many of the emerging economies this past year. The Asian crisis of 1997 had already rocked the global marketplace and left currency crises, recession, and social and political upheaval in its wake. Although some of these economies are showing promising signs of recovery, the economic slump in Asia is still a serious concern. The picture darkened last year as Russia plunged into economic and financial turmoil; the ensuing financial instability took a particularly severe toll in August and September. These events have had many serious consequences, including a decline in commodity prices, which in many instances plummeted to thirty-year lows, and the widening of the financial spreads that emerging country borrowers have had to pay to secure new loans or roll over existing ones.

The Situation in Latin America and the Caribbean

Continuity of modernization and reform processes

We have had occasion in the past to describe our region's extraordinary recovery from the deep-seated crisis of the 1980s.

Latin American and Caribbean countries were able to stabilize their economies, closing the book on an era of fragility and devastating inflation. For many countries in the region, this has meant a return to fiscal balance and sound monetary policy, and the entrenching of market economies. The region managed to regain its place at the forefront of the emerging economies and win back the confidence of global financial markets, from which direct private investment and short-term capital flows reached some US\$65 billion in 1998.

In the process, these countries were able to move quickly to liberalize and open their economies unilaterally by reducing tariffs, easing nontariff restrictions, and launching aggressive regional integration initiatives in pursuit of a new "open regionalism."

These successful recovery efforts paved the way for modernization initiatives and structural reforms bearing on the size of the State, the liberalization of markets, and the preeminent role of private enterprise in economic activity.

There were signs in 1997, when economic growth reached an average rate of 5.5 percent, that even stronger growth was a possibility because of the expected deepening of reforms.

Against this backdrop of continuing modernization and healthy growth, there were reasonable expectations that countries would be able to craft policies to successfully combat poverty, exclusion, and unemployment, and to improve the distribution of income. Just as these legitimate expectations were taking hold—when many segments of society were beginning to show impatience after years of painful adjustment and sacrifice—the region found itself caught up in the spillover from the Asian crisis and then the financial turmoil stemming from Russia. These events severely dampened performance of the region's economy in 1998.

The Impact of the Global Crisis and Natural Disasters

The year recently ended was one of the worst our region has had to endure in decades.

- Natural disasters: El Niño caused serious damage in all the Andean countries, Ecuador and Peru being the hardest hit; Hurricane Georges raged through the Dominican Republic, leaving destruction in its wake; and Hurricane Mitch took a heavy toll in human lives and production infrastructure, the latter losses being estimated at fully two-thirds of gross domestic product in Honduras and three-fourths in Nicaragua.
- In the context of the Asian crisis unleashed in 1997, which pushed down economic growth worldwide, the Latin American and Caribbean economies saw massive withdrawals of portfolio investments and difficulty of access to international capital markets.
- World prices for the region's export commodities plummeted. Oil prices fell by 30 percent, on the back of a five percent decline the previous year. Copper prices also plunged, for a cumulative decline of over 30 percent from the last quarter of 1997. Prices for sugar, wheat, and coffee fell by more than 20 percent.

Individual economies in the region sustained damage on a variety of fronts:

- Exchange rate pressures, which for several countries meant a loss of 10 percent or more in international currency reserves.

- Tumbling security values with stock exchange declines of 30 to 50 percent at the height of the crisis (although these losses were, eventually, largely reversed).
- Interest rate hikes, in part to contain exchange rate pressures, but ultimately also a corollary of increased uncertainty and volatility.
- Lower fiscal revenues and higher public debt service payments.

When one considers the force of the external factors that played out in the global arena in 1998 and their spillover into domestic economies, the region's economic performance is encouraging. A few figures tell the story:

- The region reported 2.5 percent growth overall, or 4.5 percent if Brazil is excluded.
- Only two countries, Guyana and Jamaica, reported negative growth.
- Inflation held firm, averaging 10 percent for the region overall; only two countries, Ecuador and Venezuela, posted inflation rates higher than 20 percent

One could speculate that the serious problems that unfolded in 1998 are not fully reflected in the year-end figures, and that the brunt of the upheaval will show in 1999. But, once again, the region has surprised us with its strong showing in these early months of 1999. The crisis in Brazil, for instance, had milder aftershocks than the upheaval in Russia, as evidenced by the performance of national stock markets, interest rates, and the exchange situation in the other countries in the region, not to mention Argentina's recent bond issues in global markets. It is a regrettable fact of life that stable economies are typically less newsworthy than troubled ones.

This positive picture notwithstanding, the events of 1998 and Brazil's straits have added to Latin Americans' sense of frustration and uncertainty, and have raised fresh concerns.

The Challenges Ahead

I see five questions taking shape today in various quarters in the region. I would like to take a few moments here with you to offer some answers.

1. Are Latin America and the Caribbean equipped to deal with the instability that accompanies globalization?
2. Does it make sense, at the current juncture, for the region to hold fast to its policies of more open economies and markets?
3. In the present climate, what can the region do to combat poverty and deal with inequality?
4. Is there a future for the regional integration efforts on which our countries have embarked in recent years?
5. What will be the cost, in terms of survival of our democracies, of a failure to satisfy the social needs of the many disadvantaged Latin Americans?

A. *Can we contend with the instability that globalization brings?*

The first question is whether Latin America and the Caribbean can contend with the instability that seems to characterize globalization. As a preface to my remarks, I would remind you that although some parts of the developing world—particularly East Asia—have been more unsteady in the 1990s than in the 1980s, conditions in our region have in fact been more stable. A number of countries, it is true, have had to withstand severe shocks, among them Mexico, Argentina, and Uruguay, which were buffeted by the so-called "tequila crisis" of 1994-95, and some countries are weathering serious upheavals as we speak. But, unlike the widespread disturbances of the 1980s, these more recent crises have been confined to a handful of countries. Fears of a domino effect in the region have proven to be baseless, and there appears to be no wholesale drift toward instability or recession.

What this suggests is that Latin American and Caribbean countries are anything but defenseless in the face of global volatility. It is by now common wisdom that sound fiscal policy and orthodox monetary and financial management are a *sine qua non* for stability. But another tenet is gaining currency: the old orthodoxy, it posits, is not enough; to put it another way, in a world where liquidity can change from one day to the next and confidence is gained and withdrawn just as quickly, it is simply not enough for a country to be solvent. Countries also need to build defenses against financial swells—too much liquidity one day, none the next. Sometimes our countries' future is viewed with unbridled optimism only to be followed closely by apocalyptic pronouncements.

This is not the time to go into details as to the form such defenses might take to assure liquidity and credibility, but I would like to sketch out some general ideas. One necessary condition to assure proper management of the treasury is a public debt maturity profile spread out comfortably over time. Countries need contingency funds, and the treasury needs to be able to tap into liquid reserves. The liquidity of domestic financial institutions also needs to be safeguarded, by way of adequate reserve requirements and assured external support arrangements, such as access to standby lines of credit. Several countries in the region have come up with innovative approaches and have done a great deal to shore up their lines of defense, with impressive results.

As for the credibility question, we well know that countries become credible not by making promises but by taking action to make sure that past mistakes will not be repeated. A country with a history of fiscal or monetary imbalances must do more than produce healthy results, which could prove to be fleeting. It needs to adopt concrete, lasting fiscal, exchange rate, and monetary rules and institutions; obviously, this cannot happen overnight.

This does not mean that our region should content itself with the international financial status quo. In today's global economy, countries may find themselves with no choice but to take their monetary and exchange rate arrangements back to the drawing board. Along these lines, it is gratifying to see discussion being fostered in the region on the pros and cons of various exchange rate approaches. Perhaps Latin America and the Caribbean should be exploring regional approaches with an eye to a new financial order, to see how macroeconomic policies might be made to dovetail and regional integration schemes could be advanced.

It is my belief that we should look at times of crisis as opportunities for reflection. This is precisely what has happened in recent months as the architecture of the global financial system has come under scrutiny, with much discussion of how best to avert global financial crises. It is important that a policy agenda to keep globalization from destabilizing the developing economies include regional initiatives. Moreover, we must seek avenues to ensure that our region's concerns will be duly taken into account when decisions are adopted on a new global financial architecture.

B. Do pro-market policies have a future?

A second question is whether there will be a shift toward more intervention in the operation of markets. More specifically, will countries erect or restore barriers in the belief that, in so doing, they can ward off the kind of instability that has plagued their economies recently?

To judge from the events of the past months, the answer to this question is "no." Even in the throes of the most recent global upheaval, not a single country in the region has shown signs of pulling back from the global economy: there have been no controls levied on capital movements and no barriers raised to international trade, other than some temporary and mainly administrative measures.

Indeed, work is proceeding apace in another core policy area, that of reforms to bolster the private sector's role and involvement in the economy, and to underpin the sound operation of markets. Major progress was made in 1998 in privatization programs in such countries as Argentina, Brazil, and Mexico. In the current international climate, some elements of these programs have had to be put on hold; however, the governments in question plan to pick up where they left off the moment market conditions allow. The same holds true for the financial reforms under way in the region.

All this serves to confirm, yet again, that the structural reforms of the past have proven their worth. I say "yet again" because each time a crisis has flared up in a country, it has stirred doubts about the continuity of reforms. Today, the governments and people of Latin America and the Caribbean truly understand that a more open economy, privatization, and the other structural reforms these countries have put in place to make markets operate better have been good for investment, for productivity, and for economic growth.

C. In the unstable climate that appears to be globalization's corollary, will policies to combat inequality and poverty be effective?

A third question on many minds is whether the skewed distribution of income and wealth in the region today will continue; or, posing the question another way: do globalization and efficiency compromise the hope for greater equality?

The region has good reason for posing this question:

- Economic stabilization and the recovery of growth in the 1990s have not made a dent in the incidence of poverty in the region. On the contrary, the number of people living in poverty, which had fallen steadily during the 1970s to around 90 million in 1980, stands today at 150 million or about one-third of the population. Although it is not difficult to imagine that the situation could have been worse had inflation not been tamed, no one can be complacent about the scale of poverty in our midst.
- Income distribution in the region is the most highly skewed in the world. This holds true regionwide: Costa Rica and Uruguay, for instance, have the most equitable distribution profiles in the region, relatively speaking, but the gap is far more pronounced than the world average.
- The wage gap in the region between skilled and unskilled workers is the widest in the world.
- Those of fewest means—as always—stand to suffer most from the unstable conditions prevailing in several of the region's economies at present. The impact of a macroeconomic crisis is passed on to the poor in ways that are well known. These include declining economic activity with resulting losses in employment opportunities and family income, changes in relative price structures, and reduced coverage by public services as a result of cutbacks in social spending. In response, families are forced to adopt measures in the short term whose long-term consequences are often irreversible. Child employment, school leaving, malnutrition, deferral of preventive health care and treatment, violence, family break-ups, and weakened communities are some of the results. We know that this occurred in the wake of the 1995 Mexican crisis, and it is happening again as a result of the turbulence in Asia and Russia.

The issue of inequality thus should remain at center stage at this time of global financial upheaval and macroeconomic instability in a number of countries in the region. The improvised approaches of the past clearly need to give way to policies and institutions that can equip countries to make their way through new crises.

The bright spot in this picture is that equity and efficiency are not at all mutually exclusive, according to findings of studies by our own organization and others such as the Economic Commission for Latin America and the Caribbean, the World Bank, and the Brookings Institution. However, while sound markets are necessary, it is clear that other initiatives are needed to come to grips with the problems of poverty and income inequality.

That the roots of inequality in Latin America and the Caribbean run deep is painfully evident in the educational sphere. Education is one of the great dividers in the region, clearly echoed in its social strata. Quite apart from the considerable difference in the quality of education received by the wealthy and the poor, the heads of Latin America's wealthiest 10 percent of households have, on average, three years more schooling than the next 10 percent, and seven years more schooling than heads of households in the poorest 30 percent. The problem is not always that children have no schools: in access to the early grades, Latin America is on a par with East Asia. Nor does education spending appear to be the issue: although conditions vary from one country to another, overall, Latin America and the Caribbean spend much the same on education, in the aggregate, and particularly for primary education, as other groups of countries at a similar stage of development.

A further finding of our studies is that the gap between the haves and have-nots tends to widen as overall economic conditions improve. There are a wealth of opportunities for the minority who have capital or school diplomas, and meager prospects for the others. Gaps between city and rural dwellers are widening. The more fortunate workers earn good salaries and have strong social safety nets; the vast majority make do in the informal economy. None of this is news to Latin Americans.

This lack of equal opportunity should be one of our great concerns. Experience shows us that unequal access to the means of producing income is just as serious as inequities in the income distribution itself. Where opportunities are not open to everyone, societies cannot be cohesive or political systems stable, a point to which I shall return in a moment. Just as important, the lack of opportunity for broad segments of a country's population is a constraint for its development, inasmuch as it keeps a country from making efficient use of all its resources.

However, this situation could be turned around in the coming decades. In what may be a unique demographic juncture, the region is in a position to break its legacy of inequality if it takes the right steps. In the early part of the coming century, thanks to declining birthrates, there will be a temporary increase in the share of the population that is of working age, before the percentage of elderly begins to mount. During that interval, in which a record share of the population would be producing and earning, education and job opportunities can be boosted, along with savings. The challenge will be to choose the right policies, on a variety of fronts, to make the most of this particular set of circumstances. It will be essential to ensure, for instance, that labor and social policies facilitate the entrance of women and young people into the labor force, that credit will be readily available to small-scale producers, and that education reform policies will make education systems operate better. More broadly, it is essential that every individual, every citizen, has equal access and is accorded equal treatment in dealings with the State. This will mean equitable administration of justice, transparency in decisionmaking processes, and eradication of corruption.

Countries in the region are making progress in all these areas, in some cases with Bank support. The region thus has good reason to be optimistic: we have a window of opportunity in which to resolve the problem of inequality and poverty, and we can do it. While the best conceived policies will take time to show results, the time for action is now.

D. What are the prospects for the regional integration efforts currently under way?

Regional integration in Latin America and the Caribbean is playing a central role in the processes of economic reform, modernization, and democratization. The open regionalism of the 1990s has allowed the region to deepen and widen trade liberalization, signal market-oriented commitments to investors, and lock in policy reform. It also served as a platform for export experience in manufactured goods with the associated opportunities for enhanced productivity to prepare countries for the challenges of globalization. Intraregional trade additionally has served as a cushion for uncertainties in the international economy, providing export markets for goods that confront much protection abroad and an outlet for trade when the world economy is sluggish. Indeed, in the 1990s the growth of intraregional trade consistently outperformed trade with the rest of the world.

Latin America and the Caribbean are a formidable presence in the international economy. According to International Monetary Fund figures, the region accounts for 8.8 percent of world output and 4.4 percent of global trade. Japan, by comparison, produces 7.7 percent of total world output and accounts for 7.1 percent of all international trade.

However, having observed waves of financial volatility and the instability of the adjustment processes they cause in the region, some analysts and others are asking whether even that most dynamic of our regional integration movements, the Southern Common Market (MERCOSUR), is still viable.

Obviously, integration processes may be vulnerable to the effects of financial turmoil or other shocks such as those arising from unpredictable natural disasters. However, experience shows that integration agreements, once firmly in place, are more than an umbrella for "sunny days" and are capable of "weathering storms." Fortunately, our regional integration processes can draw on a number of assets to help sustain them in these difficult times.

First, integration today is rooted in a development strategy that emphasizes progressive liberalization of trade with the rest of the world. As you know, over the last ten years external tariffs have been radically reduced and nontariff barriers eliminated, and all but one of the IDB's borrowers are now members of the World Trade Organization (WTO) and bound by its trade discipline. This commitment to open markets is further reflected in the limited and temporary measures of a protectionist nature used by countries to offset the effect of external shocks. Second, our economies have undergone radical transformations and are better placed today to respond to

the uncertainties of the world economy than they were in the mid 1980s. Finally, the rapid pace of regional integration processes created new forms of interdependence among countries with their own political legitimacy that are difficult to reverse quickly. Regional schemes also have their rules and discipline that complement and reinforce those of the multilateral trading system.

The current international context of volatile capital flows and slower growth of trade will make it difficult to maintain the momentum that has characterized integration efforts in the region during this decade. The devaluation and recession in Brazil will depress its imports and eventually boost its exports, and hence could affect the trade balances of its principal regional trading partners in MERCOSUR. However, those countries have shown a remarkable capacity for collective pragmatism in resolving trade tensions in the past, an experience which should serve them in good stead in the current situation.

While the region has seen the early benefits of open regionalism and has held its course in some trying circumstances, there is a need to further strengthen the institutional base for integration. The launching of a new millennium trade round in the WTO would serve to broaden and deepen multilateral liberalization and discipline and signal the international community's commitment to open markets. In the same vein, it is important that countries push forward the development of their regional integration schemes and hemispheric and other negotiations, such as the proposed Free Trade Area of the Americas (FTAA); the European Union's cooperative initiatives and free trade negotiations with MERCOSUR, Chile, and Mexico; as well as the participation of Chile, Mexico, and Peru in the Asia-Pacific Economic Cooperation Council (APEC). Finally, it is important that individual countries keep their markets open. In this regard, Latin America must develop more direct macroeconomic instruments to deal with fiscal and balance-of-payments disequilibria that may arise from external shocks or domestic policy errors, so that trade instruments can be freed for trade policy.

E. The stability of democracy

I shall now turn to the fifth and final question I sketched out a few moments ago: can we sustain the democratic framework that several countries have been able to rebuild in recent years? Or, as many fear, will mounting social pressures push us back to autocracy—overt or veiled—and close off forums for discussion and political opposition, just when our people have become accustomed to these democratic avenues for input, thanks to party systems and the many other channels that empower them with a voice in decisionmaking?

Here, as in all these issues, I think we should start by acknowledging the facts. Democratic forms of government have continued to flourish or have been rekindled in our borrowing member countries in recent years, unmoved by successive economic upheavals and despite very serious social problems, such as imbalanced income distribution and exclusion. At certain critical junctures, when democracy has been on the line, institutions have held firm and the citizenry has made clear its backing for the way of life these nations had won back. According to public opinion polls, the overwhelming majority of Latin Americans see democracy as the best form of government, although not everyone in every country is satisfied with how democracy or political parties may be operating.

Latin American democracies are hardly unique in confronting, from time to time, complex circumstances that prevent them from taking timely decisions to solve their problems. But, by the same token, as experience in many parts of the world has shown us, crises can also set the stage for the removal of political roadblocks, by triggering a realignment of interest groups and changes in perceptions of the costs and benefits of the status quo versus potential new policies. Several Latin American countries have weathered such situations in the past decade and democracy has emerged unscathed, albeit with some major institutional shifts and accommodations. Democracy in the region, in other words, has been put to serious tests and has come through successfully, as it will surely continue to do.

Today, however, the region's democracies are under pressure as the State tries to cope with mounting demands to reduce poverty, exclusion, and unemployment; tackle skewed income distribution; and, at the same time, combat the phenomenon of "adjustment fatigue" that comes of protracted reform efforts. As if the pressures building within their own borders were not enough, countries also must contend with unexpected external shocks that can spill over from the global marketplace.

When the economic climate can be so unsettled and poverty, exclusion, and inequality are still so much in evidence, it is hardly surprising that there would be questions about the future of democracy in our countries. There are sound reasons for such concerns: history shows us that when a political system proves incapable of rising to the challenges of the moment, authoritarian ideas at either end of the spectrum find fertile ground. But the challenges facing us today, and those that await us in the years ahead, cannot be tackled with authoritarian approaches or any other outdated prescription. The Latin American and Caribbean countries have learned this lesson, at tremendous social cost.

We should be confident now as we look toward the future. For the first time ever, and for an unprecedented length of time, all our member countries have democratically elected governments. As the next step, these electoral democracies need to become full-fledged democracies, in which the various branches of government are truly independent of one another but work in harmony. Such genuine democracies are built around solid political party systems; they have strong regulatory and oversight agencies and a professional civil service that can shield the State and public policy from the undue influence of corporate, family, or other interests. This complex apparatus has yet to be put in place in many countries. Such democracies also need to nurture the synergy that comes of cooperative relations between national and subnational governments. As a further essential component of governance there must be opportunities for the public at large to offer its input, to lay the foundation for public policies that will truly answer to the needs of the citizenry.

The Bank's Role at the Present Juncture

The inexorable effects of globalization, not to mention the turbulence of the 1995 and 1998 crises, have been felt by the region when in the throes of sweeping changes. Countries are seeking to further stabilize and modernize their economies and become players in the global marketplace. In the process, they have been looking very much to the private sector, at home and internationally.

Against this backdrop, we may well ask what the Bank can do to help, in pursuit of its core mandate of supporting economic and social development in its borrowing member countries. The responsibilities that would fall to us in this sphere complement but by no means substitute for those falling to the International Monetary Fund and the World Bank.

Lines of action

In the present circumstances, and still within the framework of the Eighth General Increase in Resources, the Bank can work with and support the region through the following lines of action.

1. Support country efforts to deepen economic reforms, particularly adjustments that will shore up fiscal systems, improve the climate for local and foreign private direct investment, and create an enabling environment for private capital flows to the region, so as to foster full participation by every segment of society, and particularly the most disadvantaged, in economic activity.
2. Support social investment, particularly to cushion the impact of the external crisis on the people of Latin America and the Caribbean. A key focus here would be support for microenterprise and small business, an area in which the Bank has a wealth of experience itself and can offer the unique facilities of the other two IDB Group arms, the Inter-American Investment Corporation and the Multilateral Investment Fund.
3. Support the strengthening of regulatory and oversight systems, notably in the banking industry, as lines of defense for countries to function in the current international climate.
4. Support country efforts to strengthen their executive, legislative, and judicial branches.
5. Support integration processes.
6. Promote the transfer of knowledge, experience, and best practices to our borrowers. This type of support, facilitating internal discussion and access by political leaders and economic agents to national and international experiences, is more important now than ever, as countries buffeted by the external crisis and the associated challenges and dislocations, and confronted with new and growing demands, find themselves rewriting their economic policies. The Bank has recently stepped up its involvement in this sphere, promoting country dialogues in various public and private forums, as well as comparative analyses of problems and solutions.

New instruments available to the Bank to lend this support

A 1998 decision by the Bank's Board of Governors left our institution better equipped to respond to the financial crisis by making available a new one-year US\$8.8 billion emergency facility that uses the institution's headroom.

The emergency line is being used in particular to cushion the impact of the current financial turbulence on economic activity generally. It will help countries deepen economic reforms and rehabilitate banks, protect social spending, and support small businesses and microenterprises. The new facility will support lines of action envisaged in the Eighth Replenishment mandates as well as provide liquidity in foreign exchange to countries requiring such assistance.

Likewise, in 1998 the Bank's Governors resolved the problem of concessional resources requirements for the next nine years, including the funds needed for the Bank to participate in debt reduction efforts in Bolivia, Guyana, and Nicaragua, with an allotment for technical cooperation as well. Moreover, there is acceptance in principle of a contingent liability to meet the cost of debt relief for Honduras, should this country become eligible.

I should like to commend all the Bank's borrowing member countries for their undertaking to transfer to the convertible currency window of the Fund for Special Operations (FSO) a total of US\$2.4 billion in FSO local currency holdings. These funds will be targeted for support mainly to the less developed of the Bank's borrowing member countries. This manifestation of solidarity is deserving of our profound appreciation and respect. The magnitude of this action can only be fully appreciated when one realizes that there is no precedent among multilateral institutions for the full burden of the provision of additional concessional resources to fall on its borrowing members.

However, this new arrangement does have one worrisome side effect: a steep reduction of funds for the Bank's regional technical cooperation program, the seminal IDB activity that embodies the deeply rooted tradition of cross-border cooperation within Latin America and the Caribbean. I would urge the Bank's member countries to activate the Technical Cooperation Fund envisaged in the Eighth General Increase in Resources. This would reposition the Bank to mobilize regional cooperation, as it has throughout its history, at every economic, social, and institutional level.

Closing Remarks

The history books will be ambivalent, at best, about the strides made by Latin America and the Caribbean in the twentieth century. Until the 1980s, our region was posting the strongest growth rates in the world, and when the figures for the century are tallied, it will no doubt figure among the fastest-growing regions in the world. But alarming indices of poverty, exclusion, and inequality have been a constant as well. These are the true challenges before us as the millennium approaches.

The region was put to a severe test in the 1980s, as it cast off obsolete economic paradigms and economies were shaken to the core by the external debt crisis. The response was swift in political and economic arenas alike. Countries embarked on sweeping structural reforms that reshaped economies and laid the groundwork for solutions to serious social problems, most of which are with us still. What these reforms did not always take into account were the risks that would be part and parcel of the globalization of trade, finance, investment, and corporate structures.

In the trade arena, it took the international community several decades to establish the World Trade Organization, and it will be some time before we see truly unfettered markets for trading goods and services the world over. In the case of capital flows, by contrast, the pace of globalization has been dizzying. The same integration that yielded unquestionable benefits for financial markets left them exposed to a new set of risks.

It became clear, in the process, that the international financial architecture would need to be revamped, this being a subject of discussion today in the Group of Seven and Bretton Woods institutions, as well as in other forums. The developing countries must have a direct and effective say in these discussions, as parties to any debate on global issues.

On the domestic front, the emerging economies found themselves lacking the kind of financial institutions and instruments to meet the new demands of global finance. Latin America had no choice therefore but to implement painful exchange rate, fiscal, and monetary adjustments to stabilize its economies and send positive signals to the global financial markets, and it did so with courage and determination. Thus, I can end this presentation on an optimistic note, confident in the region's capacity to rise to the challenges it faces in this complicated set of circumstances I have made mention of today.

It would be quite unrealistic to think that the next chapter will be an easy one. Indeed, the current year promises to be a particularly difficult one, as countries no doubt will watch their growth rates slip below 1998 levels, contend with continuing instability outside their borders, and face up to pressures that could jeopardize the continuity of their economic and social policies.

This is not the first time we have sounded a note of caution in these annual overviews of the region's performance and prospects. As far back as 1995 we warned of volatility risks and the dangers of excess credit and overspending. Precisely for that reason, over the past four years, the Bank has accorded priority support to reforms in financial systems, bank regulation and oversight, and the strengthening of fiscal institutions. At each of these annual gatherings we have also been calling attention to the sluggish pace at which the reforms are beginning to make an impact on social problems and the attendant impatience in our societies with seemingly endless adjustment.

Finally, I would like to leave you with some reflections more of a political than of an economic nature.

A fundamental reason why our region can boast one of the strongest growth rates in the twentieth century yet still have such widespread poverty and inequality is that its political systems are not functioning well. With few exceptions, our public policies have been ineffectual not because the underlying technical design is deficient, but because, in the absence of a broad democratic institutional base, it has been very difficult for governments to truly address the needs and aspirations of the citizenry. It is no coincidence that countries with the deepest-rooted democratic institutions, culture, and tradition enjoy the highest standards of living and show the highest indices of social inclusion and cohesion.

The structural flaw in the political systems has consequences at home and abroad. At home, countries cannot easily strike a balance in public policy between "economic efficiency" and "social efficiency." In other words, they cannot ensure that economic growth and social justice go hand in hand, in a truly democratic system. On the external front, the delays in, and failings of, the various moves toward integration—that perennial dream of our liberators that has lost nothing of its currency—can in part be traced directly to recurring political instability, sudden changes in government, and shifts in decades-old ground rules.

To keep pace with globalization, we have no choice but to integrate inwardly and outwardly. We will not be able to do so unless we have strong democratic systems in place. There has been much talk in recent years of values, culture, and institutions, as well there should be, but these elements are only part of the picture. There is no way around it: politics is vital to the life of a people. Institutions are more than the sum of organizational engineering elements that go into their creation and operation; they are an essential part of what we know as politics. Issues bearing on judicial reform, strengthening of parliaments, and promotion of civil society are parts of initiatives for reforming and modernizing the State, and core concerns in political reform efforts to deepen and bolster democratic systems.

In Latin America and the Caribbean today, one aspect of the strengthening of the State is decentralization of responsibility for providing many traditional public services. Central government functions are being transferred to local and other subnational governments. State-owned enterprises are being privatized and private enterprise is beginning to undertake activities that had always been the preserve of the State. Among the functions previously reserved for the central government but now the bailiwick of private enterprise and local institutions are education, public health, culture, transportation and communications, electric power, water supply and environmental sanitation, housing, and urban development.

Today local institutions, by which I mean municipalities and other subnational government agencies, have a dual role: they are advocates for citizens in their geographical area in dealings with the State and, within their own jurisdictions, they are the local articulators of State functions and responsibilities. In that capacity they have become a force for political and cultural integration.

Decentralization is essentially a political and administrative process whereby powers are shifted to new decisionmaking centers, new government jurisdictions, which must determine how to apportion the funds they raise themselves or receive as transfers from the State. Many of the decisions that affect the day-to-day life of the populace are being shifted to the local level, particularly in arenas in which the economic, social, cultural, and political elements of community life are played out. These new decision centers have taken some early initiatives, but their efforts to articulate their new responsibilities are proving to be far more daunting in restricted economic circumstances than would be the case in a climate of economic growth. The new challenges are many; the resources to address them are becoming scarcer every day.

Clearly, there is a need for new formulas for the interaction of the State and civil society, to keep pace with the changes afoot. More than ever before, this will mean working closely with local government and civil society while drawing maximum advantage from the free play of market forces. The deepening of the democratic process by developing and drawing on the strength of the social capital in our countries is imperative if the region is to take full advantage of the demographic window of opportunity to make significant inroads against poverty, inequality, discrimination, and other endemic social ills in the first decades of the new millennium.

Here again, as in the outlook for our economic progress, I see every reason to be optimistic about the future of our region.

At the outset, I would like first of all to thank Enrique Iglesias for the honor he has done me of inviting me to address this forum following his remarks this morning. Knowing him well, I wondered for a moment what reasons he might have had for inviting me. Did he want to put me to the test as one who seeks to be a prophet in his own country?... I think what he really wanted was to let you experience firsthand the closeness and warmth of the relations between our two institutions; although this is a constant, it is never more true than in difficult times such as these. But every honor has its obligations, and mine this morning is to use the working language of the IDB. I beg the French-speakers among you to forgive me, and also those of you who are Spanish-speaking, as my Spanish may grate on your ears.¹

It goes without saying that I concur wholeheartedly with the visionary and perspicacious analysis provided by President Iglesias. Allow me merely to add to his comments the experience of the IMF—an institution you have asked to take the lead in combating the crisis—and then, based on that experience, to try to respond in part to some of the questions that President Iglesias has so opportunely brought to your attention.

It is true that these last few years have taught us much about the meaning of globalization and the opportunities and risks that it entails. Your countries' experience in this area points up three important aspects:

First, your countries seized the opportunities that came their way, and, beginning in the early 1990s, attracted sizable capital flows that played a key role in the highly desirable acceleration of their growth;

Second, owing chiefly to their sustained efforts to overcome the debt crisis and to base their growth on macroeconomic stability, public deficit reduction, and structural reforms, your countries fortified themselves in such a way that they were able, collectively, to withstand the shocks delivered by the crisis and to do so in a most impressive manner—even though, of course, the effects of the crisis began to be felt in 1998 and will continue with greater severity in 1999. But I would like to highlight one aspect of their success in particular: the extraordinary resilience demonstrated by the region, which is due in large measure to the prompt, responsible reaction of policymakers in confronting the situation head-on, as well as their efforts, over the last 10 years, to implement broad reforms that have provided the region with sound financial systems and a framework of more flexible policies. It is encouraging that investors now seem to be starting to discriminate more clearly among countries, based on their individual economic strengths and the consistent focus of their economic policy;

Third, the hardest-hit countries—Mexico in 1994-95 and now Brazil—have demonstrated their ability to respond with bold programs capable of attracting vital international support and to create new bases for stronger and more sustainable growth. This is what Mexico accomplished, and we all applauded its success, and this is what we now expect of Brazil, because we all know how strong the current program is, because we are all aware of the authorities' determination to implement the program resolutely and without delay, and because we are convinced that all its partners in the highly promising task of developing this great country—be they banks, private creditors, or friendly governments—will continue their support and will appreciate the special importance of bolstering Brazil's valiant efforts in these difficult times. Confident of the supplementary funds that will be forthcoming from all its partners, in addition to our own contribution of \$18 billion, I have decided to submit the program for the approval of the Fund's Executive Board at the end of this month or in early April. The success of this program will be Brazil's, but it will also benefit Mercosur and its member countries.

What more, then, can your countries do now, when we know that 1999 will be extraordinarily difficult for all—when you are faced with repairing the damage of horrific natural disasters and adjusting to the slowing of world economic growth, falling export prices, exchange pressures, reduced external financing, and increasing interest rates and spreads? What can be done when, as a result of all this, the prospects for near-term growth have evaporated and a drop in per capita output is expected this year, with a consequent rise in poverty?

First, for individual countries, it is true that there is no quick fix and no substitute for the kind of prudent, consistent management that inspires market confidence. But what does such management consist of?

- **The relentless defense of macroeconomic stability**, with all its implications for fiscal policy, and a necessarily flexible approach to monetary policy.
- **The deepening of structural reforms**, as there is still considerable scope for pursuing privatization, increased flexibility in labor markets, and further advances in the area of banking legislation and supervision.
- And, lastly, pursuing the **second generation reforms** that your countries pioneered, with IDB and World Bank support, long before they became generalized in the international debate on the new financial architecture. It is now clear to everyone that investor confidence can be won only through good governance, transparency, and stronger market institutions.

But, as we all know, this globalized world of ours requires an additional dimension. At this point, I feel compelled to respond to President Iglesias's fourth question: "In these circumstances, do regional integration efforts have a future?" My answer is categorical:

¹ The first paragraph of the address was delivered in French.

yes, now more than ever. However, I am not going to discuss theory with you today. Instead, since we are the guests of one of the 11 countries currently in the process of creating a new currency, the Euro, which immediately established itself as the world's second reserve asset, with an impressive stabilizing and defensive effect on the economies adopting it, I would like to encourage you to take a few moments to think about this experience.

Above all, I want to stress that what we admire here today is not the result of an ingenious strategy to achieve monetary integration among economies with very similar characteristics. On the contrary, it is essentially the result of a persistent effort to achieve macroeconomic convergence, which, since the early 1980s, in a context of initially very different situations and perspectives, steadily created the conditions necessary for the adoption of a common currency. This economic integration effort is now culminating with the creation of the single currency. Of particular relevance, however, is the benefit that each of these economies has drawn, over this long interval, from these convergence efforts: that of being able to join forces to gradually root out problems created by inflationary imbalances and protectionist demands. This same route is open to all of your countries as well, to ensure the success of national efforts and reforms. Regardless of the final monetary option chosen, the convergence and regional integration of your economies is essential to the strengthening of your countries and their ability to adapt to the new international financial environment—regardless, I repeat, of the final monetary integration option chosen. The fruits of these convergence efforts—the difficulties of which I fully recognize—could be invaluable:

- They would provide further evidence of the region's determination to meet the challenges of a globalized economy and to continue managing their economies in a coherent and stable manner;
- Through an exchange of information and opinions, policymakers would be able to better assess the risks facing each country and formulate more appropriate policies;
- In addition to fostering the convergence of national policies, they would help governments consolidate domestic political support for their policies, warding off protectionist or backtracking tendencies;
- Lastly, they would offer a means of assessing the impact that policy changes in one country have on its neighbors, thus limiting the possibility of destabilizing unilateral decisions.

There are several ways of promoting such regionalism, and indeed many forums already exist. I would like to stress its importance in three areas: macroeconomic policies, finance, and trade.

I have already said enough about macroeconomics. I need only add that just as the International Monetary Fund makes itself available to the G-7 and other groups and regions, it is there to assist you in your efforts to facilitate a frank and open regional discussion of the economic policies being implemented. A convincing first step in this direction was taken last September when finance ministers and central bank governors from Latin American economies with regular access to financial markets met at Fund headquarters in Washington to discuss their situation and policy options in the aftermath of the Russian crisis. This experience could be expanded to periodic meetings, with broader representation and with countries possibly organized into subregions to ensure the active participation of all. Such meetings would provide fertile ground for the discussion of novel ideas and for gradual policy convergence.

Second, you may wish to consider a coordinated regional approach to financial supervision. If any lesson has emerged from the crises of the past few years, it is the necessity of decisively strengthening financial systems. The Basle Core Principles for Effective Banking Supervision represent an important step toward defining standards that are applicable throughout the world. I urge Latin America and the Caribbean to put these principles into practice as quickly as possible. But could you not go one step further? To give a strong boost to confidence in the region, why not consider complementary regulatory measures better attuned to the specific circumstances of the region? Let me give you one example: The Basle Core Principles recommend a minimum capital adequacy ratio, duly weighted for risk. But as the exposure of banks in the region may be greater than among more diversified international banks, a higher ratio may be needed, and indeed some countries have already come to that decision. Other regulatory issues such as accounting standards and portfolio valuation, or the proper criteria to assess banks' internal risk management policies, also could benefit from a regional definition based on international principles, adjusted to regional circumstances. All these aspects could in turn benefit from closer cooperation between national supervisors and renewed efforts on the part of the regional association of supervisors, with ongoing support from the IDB and the IMF.

The third area is trade. Evidence continues to mount of the close links between export performance, the degree of trade liberalization, and economic development. This is a lesson learned long ago in this region and most countries have remained firmly committed to open trade regimes. Indeed, progress has continued towards a further reduction in tariffs, including through the launching of the negotiations for the Free Trade Area of the Americas. However, in times of crisis, the risk of trade tensions increases. Trade policy can never be—nor should it be—used as a substitute for macroeconomic policy adjustment, and it is essential that we keep trade liberalization at the forefront of governments' agendas. I have no doubt that countries in the region will continue to eschew protectionism and will avail themselves of existing regional mechanisms, such as Mercosur, to preserve and accelerate the liberalization of their economies. Regional trade liberalization initiatives can offer important benefits, but we must avoid the disorderly proliferation of overlapping and sometimes conflicting regional trade arrangements. It is therefore essential that we promote dialogue and make certain that regional initiatives progress in a decisive and nondiscriminatory manner toward the liberalization of trade.

I feel certain that your responses to this very important question will be far more imaginative than my own. Allow me, however, to answer another question, which is surely on many people's minds: what does the IMF plan to do in these difficult times to help the IDB support its member countries? First, we will, of course, continue doing our utmost to fulfill our traditional role, and, in particular, to increase our support to the 11 countries which already have or which are negotiating programs with us, representing total commitments of as much as SDR 21 billion (US\$28 billion). What this means now is bringing discussions to a successful conclusion,

particularly those with Ecuador and Venezuela, and playing as active a role as possible in assisting the victims of Hurricane Mitch, to mention only a few programs. But beyond this, our mission is to contribute to the international community's efforts to find the most appropriate response to the poorest countries' severe debt problem and to create a new capability to enable us to grant contingent lines of credit to countries which, despite prudent macroeconomic management, are vulnerable to the volatility of financial flows. In this way, we hope to have a catalytic effect, facilitating the creation of the banking lines of defense that President Iglesias mentioned. Indeed, this new approach could be one of the first components of the new architecture of the international financial system, which the Interim Committee will discuss in Washington at the end of next month. The objective of this discussion should be to provide your countries with the stable, equitable framework necessary for sustainable, high-quality growth.

This is a time of great challenges for Latin America and the Caribbean. But when I reflect on the courage of the people and governments of this great region—whether it is the efforts of the countries hit by financial turbulence to withstand contagion, the indomitable spirit of the people of Central America as they rebuild from the destruction of Hurricane Mitch, or the tenacity of the island nations of the Caribbean in the face of a difficult external situation—I am convinced that the region will progress to even greater heights and will be strengthened by this crisis. And rest assured that we at the IMF will do all we can, in close cooperation with the IDB, to make that come to pass.

The IDB's invitation to this forum every year gives us the opportunity for free and open reflection, which is always welcomed in the ecumenical atmosphere that characterizes the work of Enrique Iglesias. During our deliberations today, I would like to change the focus. Rather than merely enumerate the mix of policies and remedies appropriate to today's circumstances, I propose to think out loud on some of the questions cropping up here and there, which no one seems to feel obliged to answer—or to answer as conclusively as usual—because we have lost much of our certainty. Every day seems to bring more of these new questions, adding to the previous day's, which we have not even begun to answer.

The question before us today is: what has caused the great volatility in capital flows that seems to be the most undesirable characteristic of globalization thus far? Is the contagion effect an unstoppable phenomenon that will overwhelm the markets without restraint or compassion? What do we really think of Professor Krugman's suggestions about returning to exchange controls? Can we go back to a system where emerging economies have someone across the table with whom to discuss debt rescheduling? Can we move towards a more secure international financial system? Weren't all the reform proposals thwarted when the fixed exchange rate system was eliminated? Or when the so-called debt crisis erupted? Are we capable of maintaining national sovereignty, a better regulated and supervised international system, and a global capital system simultaneously? Are an international bankruptcy court, or a global bank, or a global regulatory agency in our future?

The doubts, concerns, fears, and proposals that abound are compounded by a process of mutual recriminations. The message from the markets is that information and transparency are inadequate and the adjustment process too slow. It is as if an increasingly pent-up sense of impatience were suddenly vented. At the same time, governments are being accused from all sides of sacrificing growth unnecessarily, raising interest rates excessively, destroying the social safety net for our poor and disadvantaged, and protecting bankers at the expense of society's weakest members.

In the panic of the moment, our markets systematically overreact without distinction between good policies and bad ones, temporary adjustments and structural ones, sound companies and unsound ones.

Strong voices in the media and among important public figures are taking the IMF, the World Bank, and all multilateral economic institutions to task and urging them to discuss their policies openly and publicly. Other voices, like the *Wall Street Journal* or George Shultz now call for the elimination of such institutions. And this time, the harshest opinions come not from some maladjusted leftist intellectuals or third world leaders but from distinguished economists, giving the impression that all economic and financial orthodoxy has suddenly disappeared. In reaching such conclusions, good arguments are likely mixed with foolish ones.

But Professors Sachs and Krugman—and the *Wall Street Journal* itself—are clearly the cream of the academic establishment, and their diverging opinions can no longer be silenced by authoritative pronouncements. I personally do not share their views but they have made us stop and think, made us doubt; their statements require judicious responses and can only be validated or refuted as events unfold, as is the Malaysian experience, for example.

It is also disconcerting that the economic policies of certain powers are, in the main, being criticized not by remnants of the Marxist left but by the economic authorities of their main trading partner, as in the case of Japan.

Moreover, uncertainties doubtless extend beyond mere economic concerns:

- Are there features of the new model—which some like to call neoliberal—that are intrinsically unfair, that do not eliminate poverty or that actually work against the poor?
- Will the model always and inevitably be deemed to worsen income distribution?
- Do the technocrats really care about social policy or education or health?
- Will the merger process now fashionable reawaken the threat of monopoly long dormant during the upsurge in domestic and international competition?

Or, turning to other topics, what is happening with crime in Latin America and the Caribbean, where average homicide rates have doubled over the last decade, seeming to nullify efforts towards justice system reform and investments in domestic security?

Every day we seem to be farther from, not closer to an educational system that can help us face the problems of our disadvantaged while preparing us for the challenges of globalization.

Accusations of corruption have also multiplied. Is this because there is now greater freedom to air them? Or has globalization brought corruption in its wake? Or is it a product of greater democracy and civil liberties?

And what can we say about the dangers to our culture, which seems to evaporate before the onrush of globalization—a concern no doubt to those who have come to talk about culture and development.

And how can we communicate all these doubts in a simple question? How can we move beyond our perplexity at such a panorama—beyond the fear of change, the desire to retreat into our own concerns or into a nostalgic vision of the past? The problem

is that these episodes are not only disconcerting for our citizens, or for labor or industry—they are disconcerting for the very political and economic leaders who must make decisions in our countries every day. Nor does academia seem to have the answers. In our current situation, all we seem to encounter in that quarter is more questions.

The time has therefore come to set fear aside and begin, today in this very forum, to search for more orderly, more collective, and more meaningful answers, to help renew our faith in the path we have chosen towards modernization and reform. That is the only way to seize the opportunities inherent in globalization, while avoiding its harmful side effects.

The elitist, closed, and overly economic approach of “the Washington Consensus” must give way to such an effort. The old model has proven too authoritarian, too jealously guarded, and too dogmatic—a matter of faith not easily questioned in public debate. Its relevance, moreover, has been completely overtaken by the events of recent years, and only a few fragments of it can be preserved.

The wisdom and remedies of that old model must now be replaced by a broader, more political approach, based on a wider social consensus, participation by many more interest groups and sectors and a better understanding of the modern media, technology, civil society, and our increasing economic, political, and social interdependence. For example, determining how to support a country having problems is no longer a matter reserved for economists or investment “gurus.” Judgments based on solid technical knowledge are of course important, but so are public opinion, surveys, and political positioning, as we saw during the 1995 Mexican crisis.

We need better international regulations—more of the IMF rather than less—with a stronger mandate, better qualified staff, greater transparency and accessibility, far more resources, and policies formed through open debate. Some of the Fund’s old “prescriptions,” as they are affectionately called by economists, remain valid. There is a certain measure of bad faith in maligning the Fund’s programs while ignoring the fact that better programs will most probably require more, not fewer, resources. But it is also true that the Fund’s role in protecting international investors and banks needs some careful reconsideration. The excessive secrecy, for instance, is no longer acceptable. The problems in Asia are also being reinterpreted as a failure to anticipate the chain reaction in world markets. And it has become clear that capital mobility is incompatible with weak financial systems.

During periods of retrenchment, when markets become more conservative and less liquid, conditions demanded by investors surpass the orthodoxy of the Fund and the Bank themselves, which makes it more difficult for our leaders to reach judicious policy decisions and for the Fund and Bank to explain or justify disproportionate market reactions.

A more efficient State, with greater regulatory power, better justice and education systems, and a better social safety net, is increasingly in demand. In the 1980s, the new agenda was greater trust in market mechanisms; we must now turn our attention to the new responsibilities of the State.

To make privatization such a major component of the policy discussion is to be caught in an outdated and simply ideological debate, for its opponents as well as its supporters. It is time to shift our focus from those themes to more important institutional issues: the State and its role in economic development. This is not exactly a new topic, but one that has taken on new relevance.

But to turn now from these digressions and come back to the Washington Consensus, the new responses, the new agenda must transcend our perspective as bankers and embrace a much broader range of interests, where political parties and leaders play a central role, and—for all their limitations and flaws—are the first to contend with the surprises sprung by markets or governments. They are perhaps the only ones able to convey messages far more complex today than in the past.

The other thing we can be certain of is that no one is going to perform the task for us of answering the complex questions we face today. No one possesses the wisdom that certain institutions and individuals had in the past. Today, our efforts must be much more collective, much more comprehensive. We will no doubt make mistakes and learn the hard way, just as we have unequivocally done during these recent years of financial turmoil. To everyone’s (and our own) surprise, it has been more difficult to find a good set of policies than it has to rally vigorous political support behind the policies we have tried on many occasions.

My thanks again to Enrique Iglesias and to the IDB for providing a forum for these comments. We hope that the OAS will be able to contribute to the discussion on the new agenda and to the search for a new consensus. I believe the organization is particularly well placed to do so during this time of integration and collective action.

A year ago, when the Board of Governors of IDB met in Cartagena, the international financial crisis that had broken out in Asia was beginning to make itself felt in Latin America and the Caribbean. World financial markets were starting to rebound at that time, however, and this buoyed our hopes that the impact of the crisis on our region would be fairly mild. These hopes were not borne out. The even greater disturbances experienced in the international capital market in the wake of the Russian moratorium of August 1998 have been compounded by the uncertainty that has arisen as a result of the industrialized countries' delay in finding effective means of coping with the crisis and the sharp downturn in raw material prices on the international market. This has triggered an economic slowdown and has propelled a number of the medium-sized and large countries in our region into outright recession.

In seeking to deal with this difficult situation, during the past year and a half the region's economic authorities have displayed a degree of determination to implement adjustment measures of a magnitude perhaps never before seen in the region's history. We are therefore convinced that, given a favorable international economic environment, our region will soon extricate itself from its present difficulties. There is no question as to the fact that the scope of the disturbances experienced by the region is a reflection of serious flaws in the international financial order and particularly of the marked asymmetry existing between an increasingly sophisticated, yet unstable, international financial system and the institutions that regulate it. In short, the world lacks the types of institutions that financial globalization requires.

There is a growing awareness of this fact at the international level, where the discussion of these issues has given rise to a consensus on a number of issues. These areas of agreement are reflected in the statements issued by the Group of Seven, the Heads of State and Government of our region, the International Monetary Fund and other international organizations, including a document recently drafted by the economic and social agencies of the United Nations in whose preparation ECLAC played an important role. There is consensus as to the need for the industrialized countries to maintain expansionary policies so long as the present financial uncertainty persists and for contingency financing to be made available to buttress troubled economies before --rather than after-- their international reserves reach critically low levels. There is also a basic agreement about the wisdom of improving the flow of information, developing international codes of conduct in various areas and upgrading prudential regulation and supervision at the global level; there are still, nonetheless, many differences of opinion as to which institutions should be entrusted with this responsibility at the international level. A consensus also exists as to the need for more effective oversight of all countries' macroeconomic policies, especially during the bouts of financial euphoria that engender such crises, and for a means of ensuring that the industrialized countries' macroeconomic policies will be consistent with the objective of stable, non-inflationary growth for the world economy.

Just as importantly, today it is widely recognized that programs aimed at liberalizing the capital account must be properly sequenced and must be implemented cautiously, especially in relation to short-term flows. There is also an awareness that strong prudential regulation and oversight mechanisms at the national level are a prerequisite for any such process and that, whatever the nature of the international rules that are instituted in this sphere, they must include safeguards for coping with difficult circumstances. The international community has also recognized the need to establish orderly debt workout mechanisms to deal with critical external debt problems and to ensure an equitable distribution of the burden of adjustments. And there is also a broad consensus as to the need to strengthen our social safety nets to protect the vulnerable groups in society from the harmful effects of adjustment processes. I must also note, however, that this last tenet has thus far advanced primarily in terms of rhetoric rather than in actual practice.

Alongside these important areas of consensus, however, there are many differences of opinion, some of which are of vital concern to the developing countries. I would like to refer briefly to five of them here. The first and foremost of these issues is the financing of contingency mechanisms. The periodic contributions made by industrialized nations to IMF or for specific contingency loans have proven to be a highly unreliable funding mechanism. Under these circumstances, it is clear that we need to design much more reliable instruments to respond rapidly to the demand for additional liquidity in times of crisis. The active use of special drawing rights for this purpose would surely be the best way of doing so. In fact, and this is my second point, the active use of special drawing rights in international finance is of the utmost importance to developing countries. The current state of affairs should therefore serve to restore this instrument to the central role that it should play in the international financial order.

The third issue is the most controversial of all. Outside of an influential circle, the consensus view is that the conditionality of the International Monetary Fund has been carried beyond what can be perhaps considered reasonable bounds. It has, in particular, been extended to include questions relating to economic and social development institutions and strategies, which fall within the purview of other international organizations and of legitimate national authorities, and should be founded upon broad-based social pacts. Thus, the current discussion should also help us to arrive at a new agreement as to the limits of that conditionality, which will, in turn, endow it with the required legitimacy. The fourth point I would like to make here is that, so long as we lack an adequate order and, most importantly, clear-cut rules regarding access to appropriate amounts of contingency financing, the developing countries should, in our view, maintain their autonomy in the management of their capital accounts.

Finally, the present situation provides an invaluable opportunity for re-thinking the role of regional and subregional financial institutions. We are convinced that an international financial order that is based on a network of regional and subregional reserve funds and development banks, rather than on a few international organizations, will contribute not only to the stability of the world economy but also to more equitable conditions at the global level. Latin America and the Caribbean should therefore work to strengthen existing regional and subregional financial agencies and to complement them with new mechanism of cooperation in this area.

Distinguished Members of the Board of Executive Directors, Members of the Board of Governors and Chairmen:

The crisis has given us the chance to re-think the entire world financial order and to use that collective analysis as a basis for more effective and more balanced forms of international cooperation. In addition to offering our ongoing collaboration in this task, I would like to emphasize the fact that the Inter-American Development Bank and the eminent Latin American who presides over it, Enrique Iglesias, are also natural leaders of such an effort. I would also like to underscore to the leadership role that France has played throughout the past year on this front, which makes this great nation, held in such high esteem by the Latin American and Caribbean region, a strategic partner in the reforms that the developing world is entitled to demand to ensure a more appropriate international financial order.

France is pleased to welcome this meeting of the Inter-American Development Bank. We can measure the prestige of this institution by the distinguished figures who have honoured us with their presence. Today the Bank plays a prominent role in the life of the international community, as it celebrates its 40 years of existence—40 successful years in the service of development in Latin America and the Caribbean.

The countries of Latin America strove ardently to create this institution. And we Europeans believed in it from the outset and have joined its major shareholders.

Since 1959, the Inter-American Development Bank has established itself on the international economic and financial scene. It has responded to your demands and provided you with the necessary funding. It has understood that development must benefit people. It has given full weight to the social dimension of growth. And it has worked to strengthen public institutions. Today, it knows that the great challenge for the future is to give people access to education.

Throughout all these years, the Inter-American Development Bank has kept its innovative spirit and exacting standards intact, as well as its capacity to respond immediately as the situation requires.

Yes, the development of Latin America and the Caribbean, the spectacular emergence of so many of your countries, and the consolidation of their success, owes much to the Inter-American Development Bank. And to its President, Mr. Enrique Iglesias, to whom I wish to express our esteem and our gratitude, and I know I speak for you all.

Enrique, my friend, we know each other well. I know how much energy and conviction you bring to the service of what is for you not so much a mission as a humanistic ideal. With you at the helm, the Bank is in good hands.

Today, your institution and the countries it supports are experiencing the backlash of the grave financial crisis, the first real crisis of globalization, which originated in Asia two years ago.

I am only too well aware of the painful consequences this is having on certain of your countries and your peoples. But I am confident. I know that your economies are now built on solid foundations, thanks to the reforms accomplished.

In my visits to Latin America, I have seen for myself the renewal and the rich fabric of your democracies, the vitality of economies restored to health, and the quality of your programmes to roll back poverty. You have successfully broken with the forces of conservatism and modernized your societies.

Today, your economies have the capacity to weather "heavy storms". They are led by men of conviction and strong will. I know the resolution of my friend President Fernando Enrique Cardoso and I am confident in Brazil's economic programme. I know the tenacity and courage of my friend President Carlos Menem, as well as yours—my dear friends Eduardo Frei and Julio María Sanguinetti—and of your leaders in other countries.

Crises put solidarity to the test. Over many years now, Latin America and the Caribbean have made remarkable efforts to strengthen their regional integration. That is the way of the future. The only way. The current difficulties must not be allowed to throw you off course. That is the lesson we in Europe have learned from crises past.

But the entire international community needs to be mobilized. We must act together so that the necessary reforms in the international financial system can be implemented in 1999. This is not about calling globalization into question. Having built your development on open world markets, you know that the solution will not come from withdrawing into yourselves, from a return to protectionism, for we would all suffer from that. We will never be rid of crises, but we can prevent them or limit their effects. To that end, the international financial system needs to be made more stable.

France has already formulated a certain number of proposals on that score. I won't dwell on them here. Nevertheless, I would like to recall the responsibilities of the private sector. One cannot expect public institutions to do everything. States, and the major international institutions, including your own, cannot by themselves bear the entire burden of resolving crises. Private creditors must also become involved.

But I also want to say that we will not be able to reform the international monetary system and make it more stable without the consent of all. That is why France has proposed a summit in Paris, if possible this autumn, to be attended notably by the heads of State and Government of the IMF Interim Committee's member countries, so that together they can solemnly adopt the reforms our system needs.

As key players in the world economy and directly concerned by these questions, Latin America and the Caribbean should be present too. That is the whole point of this initiative. We need your advice and your experience.

But the answer to the present difficulties must also contain a social dimension. These crises are gravely impacting the living conditions of millions of men and women, and they could even jeopardise the very future of democracy.

We must fight poverty to ensure that globalization leaves nobody by the wayside. And we must ensure effective solidarity among nations.

France is the G7's largest aid donor in proportion to its national wealth, and the second-largest in the world in absolute terms, behind Japan. It accounts for 20% of all aid provided by the European Union, which in turn is the largest official aid donor in Latin America. It relentlessly pleads in every forum for an increase in development aid, particularly for the poorest countries.

Hurricane Mitch was met by a tremendous upsurge of solidarity. I visited the area a few days after the hurricane, seeing for myself the immense human devastation in the four countries affected. The situation called for an exceptional response. The international community responded to your appeal, Mr. President, and marshaled powerful support. In addition to its immediate financial aid, France cancelled the totality of its official aid debt claims on the devastated countries. Since then, Paris Club creditors have granted generous treatment for the next three years.

Beyond these emergency situations, I would like to see a definitive solution found at last to the ever-recurring problem of debt. The G7 summit in Lyons, in 1996, made significant progress, but we need to go further. That is the thinking behind the proposals put forward by France for the forthcoming G7 summit in Cologne. They are precise proposals, based on the principles of generosity, equity, and responsibility.

Generosity, to begin with. Bilateral debt cancellation should exceed 80% for the poorest countries. Concessionary solutions must be worked out for the other countries burdened by unsustainable debt. We also need to find a solution to the problem of multilateral debt for those countries that need it, even if that means selling off a part of the IMF's gold reserves if necessary.

Next, equity. All creditors must contribute to this exceptional effort. The burden must not fall exclusively on those countries that have provided the most substantial financial support to the poorest economies in the past. The burden must be spread among all countries in proportion to their wealth.

Finally, responsibility. This gesture must be devoted entirely to development, with as its counterpart sound management and good governance.

Mr. President, I salute your institution's commitment to a model of development that respects national identity and the human soul. That is precisely what is on the agenda of your 40th Annual Meeting. It is also one of the great challenges of the future: how to reconcile development with authentic culture; to make a success of globalization by giving training and work to all men and women, and a better quality of life, allowing them to preserve their language, traditions and values.

There is nothing more important than roots, memory, history; these are each human being's intimate compass bearings, the building blocks of their deepest being. The danger, at this time of globalization, is uniformity, a single language, a single culture, a one and only lifestyle imposing itself everywhere. Throughout its history, human beings have been enriched by dialogue between peoples, by the confluence of differences and the mingling of different sensibilities! The cultural vigour of our two continents should combine to ensure diversity in tomorrow's world!

France also encourages, and we have often spoken of this, Mr. President, recognition of indigenous peoples, so that the future does not signify for them extinction of their ancestral way of life, the death of thousand year-old civilizations, the loss of an inestimable cultural and human heritage of which our world is in such dire need. That is why France is giving substantial aid to your Bank's fund for indigenous peoples.

All these questions will naturally be at the heart of our great Summit in Rio. For the first time in history, and at France's instigation, the heads of State and Government of Latin America, the Caribbean and the European Union will be coming together next June.

They will give new and ambitious impetus to the longstanding and close ties that bind our countries. They will build a great economic, political and cultural partnership for the 21st century, by bringing together our great regional groupings which are now emerging as focal points of peace and democracy, stability and progress.

In the economic sphere, the European Union is already South America's leading trade partner, investor, and aid donor, and this situation is set to become even more pronounced. We must draw all of the appropriate consequences in terms of the agreements between our two groupings.

More and more of our banks and businesses are opening up for business in your countries. Cross-shareholdings are proliferating; hence the importance of bodies to provide support for private investment. With that in mind, I welcome the decision of the Bank to step up its co-financing with the private sector and the decision of its shareholders to strengthen the capital of the Inter-American Investment Corporation.

The Inter-American Development Bank is an essential link in this integration process. And your presence here in Paris today, for the 40th anniversary of your institution, is a powerful illustration of our common determination to enter the next millennium together.

Mr. President, as you commence your proceedings, I want to reiterate France's confidence and gratitude for everything you yourself and all of your staff are doing to develop Latin America and the Caribbean and strengthen the fraternal bonds between our peoples.

I wish every success to all Ministers, Governors and Delegates attending this Annual Meeting.

ADDRESSES

SECOND PLENARY SESSION

MARCH 15, 1999

Enrique, congratulations on another year of your successful leadership—with the Bank's prompt and successful response to financial crises, the IIC back on track and the FSO funds agreement finally resolved. Burke, welcome. We look forward to working with you.

It is good that our Bank is strong because the challenges it must meet are formidable. Inclusive prosperity that works for all, integration that supports growth and brings our Hemisphere together and strengthening each of our democracies—these were our central challenges in Guadalajara and they are our central challenges today. But to meet those goals our immediate priority after the events of the past year must be to maintain our forward momentum. So, rather than stressing these broader themes today, I want to focus on the narrower financial aspect.

Stable finance will not alone educate our children, protect our environment or build our nations. But these things cannot happen without stable finance that tames the cycle of financial boom and bust that has been part of this region's history far too often—for far too long. Now more than ever, if the gains of the past decade are to be preserved, we must work together to build Latin American confidence in finance—and build financial confidence in Latin America.

What will this require? Above all, it will mean planning for the long term. If governments live day by day, so will investors. The best financial managers hope for the best—but plan for the worst. Finance ministers and multilateral development banks (MDBs) need to take the same approach. They need policies that will serve them in bad times as well as good. This past year, many in Latin America have again been learning this lesson the hard way.

The Return of Volatility

A year ago in Cartagena, we all took cautious good cheer from the fact that the first six months of the Asian crisis had mainly passed Latin America by. Looking around the Hemisphere today we can see that our caution was well-grounded:

- We have seen events in Brazil that challenged the region's largest economy in its vital commitment to low inflation and steady growth and sent unwelcome tremors through several of the region's markets.
- We have seen the return of roller coaster inflows of foreign capital. In 1997 around US\$37 billion in net lending flowed into the eight largest economies in the region and was running at an even faster pace until the Russian crisis last summer. Today, one prominent private forecaster is predicting a net inflow of a just US\$5 billion this year.
- We have seen another dramatic downward spiral in commodity prices. This has inflicted major terms of trade shocks on Chile, Venezuela, Mexico, Ecuador and others—costing, in some cases, more than 5% of GDP.
- And we have seen major natural disasters in countries that had already seen more than their share: with hurricanes hitting Honduras, Nicaragua, El Salvador, Guatemala, the Dominican Republic and Haiti, floods from El Niño and another tragic earthquake in Colombia. We in the United States are very aware that a disaster of comparable scale to Hurricane Mitch in our own country would do more than US\$3 trillion worth of damage and cost around 500,000 lives: more than the number lost in all of our wars this century combined.

These major shocks will take their toll on the region for some time to come and no country will be left untouched. But past policies made some countries more vulnerable to these shocks than others. And the decisions governments take today will shape their capacity to contain them:

- In Mexico, Argentina and Chile, a steady commitment to stable macroeconomic policy, strengthened financial markets and careful planning have provided some important resilience to contagion and helped contain its effects. Further steps to build up these economies' defenses will only help them continue to ride out the storm.
- Brazil can succeed only with resolute pursuit of sound and strong fiscal and monetary policies. But these steps, along with the removal of past exchange rate pressures and the return of capital as normal conditions are restored, should provide a basis for the reestablishment of confidence and growth in a country that, on some measures, achieved the fastest average rate of growth in the world in the hundred years before 1980. In this context, the indications of support for sound policies in Brazil that have been received in recent days from both the private and the public sector have been encouraging.
- Other economies, notably Ecuador, will face perhaps even steeper challenges in the months ahead as they work to achieve stability. What will be critical will be to resist mis-diagnosis. It would be a mistake if the external element allowed the more important and fixable domestic roots of the crisis to go unaddressed.
- For the countries where the destruction has been greatest, help cannot come too soon. We can all take pride in the fact that, among other things, the FSO funds agreement has allowed the IDB to commit major new funds to rebuilding Central America. Let me recognize and applaud the solidarity shown by borrowers, whose conversion of FSO local currency will make this commitment a reality. For its part, the United States is willing to increase the pace of encashments of its FSO contribution to further support these ends.

Building Financial Confidence

At this time when the global economy is weak and growth is imbalanced, the goal of sustaining financial confidence—and the flow of capital that confidence can bring—is a goal for Latin America that is a goal that all can share.

However, in this region especially, our goal must not and cannot be to play the same record over. It is not enough for us to act to revive confidence today; this time we must show we have the means to maintain that confidence tomorrow.

What will this require? I would focus on four core elements:

Prudent Public Management of Risk

The first is adapting countries' financial policies to the challenge of better developed financial markets than we have ever had globally before. That means governments guarding against the risks that the speed and dynamism of these markets can create. And it means their taking better advantage of the opportunities for better spreading and managing those risks that have been created at the same time.

That means more prudent debt management. We now know that countries are courting trouble when they reach for cheap short-term capital. We saw it in Mexico, with the increasing resort to issuing dollar-denominated *Tesobonos* in 1994, and we saw it in Russia in the encouragement of foreign purchases of domestic GKO's. Countries in this region need to think long and hard about the structure of their liabilities, their exposure to rollover and other risks; and about new structures that share more risk with lenders. And they need to recall that longer term debt is the simplest and best kind of insurance of all.

At the same time we need to recognize that, while modern financial markets offer less room to err, they equally provide greater scope to plan and prepare. A modern financial planner looks to the futures markets when looking to reduce the company's exposure to price swings. Especially in Latin American countries so exposed to interest rate, foreign exchange and commodity price swings, finance ministries should be thinking along the same lines, looking for ways to spread or hedge against the risks to which government budgets and the economy as a whole are exposed. And nowhere will innovation be more welcome than when it comes to mechanisms to dampen the effects of feast-to-famine swings in commodity markets. The crude stockpiling or price control approaches that were tried in the past have long since been discredited. But commodity price-based fiscal stabilization funds, such as Chile's CODELCO, mark a different and more promising approach which other commodity-dependent nations should explore.

The IDB and other multilateral development banks can help countries' efforts in all these areas: first, by providing greater technical assistance to public officials to help them analyze, understand and respond to the risks in their national balance sheets, and second, by helping governments overcome domestic reluctance to pay the price of such insurance, by supporting appropriate public debt management and hedging programs in MDB lending operations. The IDB's work in Venezuela exemplifies this idea. So does the World Bank's recent work to give countries the opportunity to enter into hedges to offset certain types of exposure created by World Bank project lending.

Deeper Flows of Capital

Building resilience to crises is partly about better management of public balance sheets. But equally important is the resilience of the domestic financial market. Notably:

- Countries need to pursue pension and other reforms that promote higher domestic savings and more efficient domestic investment. While we think of the global capital market when we think about Latin America, the most important capital market is the one at home. A country with a broader, deeper domestic financial market is less prone to external risks and less dependent on external funds. In all of our nations, more domestic savings, better channeled, is the best route to faster growth and greater stability.
- They need to accelerate the pace of creating a domestic financial infrastructure that is more conducive to absorbing the right kind of capital. That means developing a sound financial infrastructure built on effective supervision and regulation and appropriate prudential management. And it means transparent accounting and corporate governance and effective domestic bankruptcy regimes.

Private foreign financial sector participation can and already does support these goals in Latin America. Today fully 50 percent of the banking sector, 70 percent of private banks, in Argentina are foreign-controlled, compared to 30 percent in 1994. In Mexico more than one fifth of banking sector assets are foreign-controlled. As these countries are learning, the result is a deeper, more efficient financial market—and external investors with a greater stake in staying put.

And the international financial institutions have their own critical role to play. Let me applaud the IDB and MIF's support for the work of the Committee on Hemispheric Financial Issues created at the Summit of the Americas in Miami in 1994. And let me urge them to continue with their efforts to disseminate application of the Basle Core Principles for banking supervisors across the region and help develop key parts of the infrastructure for stronger, more efficient national financial markets.

Appropriate Tools for Crisis Response

Preparing for crisis is also about preparing effective ways to respond to crises. Governments in Latin America—and the international community as a whole—need to be sure they have modern tools to respond to modern crises, and, critically, more effective tools to protect people from their effects.

The IDB, in line with similar innovations by the IMF and the World Bank, has taken an important step here with the creation of conditioned, fast-disbursing premium interest rate emergency loans—for Argentina, Colombia and most recently, Brazil—to help defend against the runs on confidence that modern capital markets can produce. Looking forward, the IDB and other MDBs need to think about further expanding their lending instruments, in two ways.

First, they could further encourage strong policies—before crisis strikes—by providing some backstop for private contingent facilities that countries develop to protect against contagion, such as those pioneered by Mexico and Argentina. Any MDB participation in such facilities will need to be appropriately designed and priced, and will need to be approached carefully, and with an eye to the headroom and reserve requirements that could cause it to crowd out other lending. But the IDB's support for Argentina's repurchase agreements with a consortium of private banks is surely a welcome new departure.

Second, we are convinced that credit enhancements, used strategically, can help to reduce the damage that a sudden loss of market access can bring. This will be an important area of innovation for the future. The use of such enhancements should be guided by a number of principles:

- They should be conditioned on strong policies;
- They should be used to maintain a well-balanced structure of governmental liabilities;
- They should be for countries trying to regain market access, not just to reduce borrowing costs;
- And, once again, they need to be appropriately designed and priced, so they leverage significant private capital without compromising the Banks' balance sheets.

These are important ideas for preventing and resolving crises involving the private sector. Other ideas are also under discussion in the international community—and the voluntary agreements entered into by Korea's private creditors and the different voluntary agreements that have been reached in Brazil's case are very welcome.

It will be important as we work through these issues going forward to remember the central irony of financial crises—that while they are usually caused by there being too much lending, they are prolonged by there being too little. To be sure, excessive flows of capital were no doubt an important element in these crises. But excess confidence in emerging markets is not a problem we face today or likely will face in the very near future. If the risk not so long ago was that investors were undertaking too many bad loans, the risk today is that they will fail to make enough good ones.

There is another, perhaps even more important aspect to MDBs' role in responding to crises: minimizing the destructive impact of crises on the crucial mission of ensuring the development and prosperity of all our people. The best—the primary—reason for wanting to respond better to crises is to lessen the economic and social distress that crises bring. But then preparing for crises has to mean preparing every member of our economy to cope with their effects.

Effective social safety nets are morally right because they provide a floor below which no one should be permitted to drop. And they make sense in narrow economic terms: because they can act as automatic stabilizers for the economy in a downturn; and because adjustments that are less painful for people are more likely to be made in good time.

The IDB has heeded President Clinton's call last September for all MDBs to step up their efforts to build effective social safety nets and promote core labor rights in this Hemisphere, but we can and must do more. As the President said, "if we want countries to do tough things, we have to protect the most defenseless people in the society and we have to protect people who get hurt when they didn't do anything wrong."

Enduring Exchange Rate Regimes

No government's search for better ways to prevent crises can overlook the place where so many past crises have begun—in the market for foreign exchange. To sustain confidence in the future, Latin America, perhaps more than most, will need exchange rate regimes that can command the trust of domestic citizens and of foreign investors, accommodate regional and global integration, and stand the test of time.

The merits of fixed versus floating exchange rates are forever debated and surely vary greatly from situation to situation. But the allure of stability in this region is strong and in that context the subject has recently arisen whether countries should dollarize.

The decision to make another country's currency one's own would be hugely consequential for any country that has to be considered in a careful and extended manner. On the one hand, dollarization offers the attractive promise of enhancing stability in the dollarizing country by adding to the credibility and discipline of its own economic and financial policies and advancing its integration with the world economy. On the other hand, the country also must be prepared to embrace that discipline—and accept the potentially significant consequences of doing without the independence to adjust the exchange rate or the direction of domestic interest rates.

While there are many issues, possibilities and approaches, it would not be appropriate for United States authorities to adjust their bank supervisory responsibilities, access to the Federal Reserve discount window, or the procedures or orientation of U.S. monetary policy in light of another country's decision to dollarize its monetary system. Any country contemplating dollarization will have to weigh carefully these considerations and many others. It will surely be appropriate that its representatives do so in consultation with the United States authorities so that we can jointly think through the implications for both of our economies.

The Enduring Agenda

There are those who say that to call on the IDB—and the international financial institutions more generally—to focus on crisis response is to distract them from their primary development mission. On the contrary, stable capital flows and sound finance are necessary to the steady economic growth on which the primary development mission of higher living standards and widening opportunities depends.

The platform of stable finance is one upon which so much can be laid—so much that will further the goals for the Americas that we laid down in our Guadalajara meeting in 1994 and the Santiago and Miami Summits. Even as the storms of crises are overhead we must not forget those goals—the goals of inclusion, integration, increased prosperity and strengthened democracies. Nor must we forget the important steps we have already taken toward them.

Looking across our Hemisphere today, I am confident that a quiet dynamic of progress has taken root in the last years of this century that will not easily be reversed. After twelve months that have seen President Clinton go to Latin America three times, visiting six countries, no one should doubt the United States's continued stake in—and commitment to—this region's success. And we look forward to celebrating our shared progress and cooperation on home ground next year when we meet in New Orleans. But every interruption is an interruption our citizens can ill afford. If the twenty-first century is to be the century of the Americas, then its final decade must continue to be the decade of Latin American reform.

In keeping with tradition, I want to start by thanking the people and Government of France for the especially warm reception they have extended us, and to congratulate them for the excellent arrangements that have been made for this meeting, the fortieth in the Bank's history. I would also like to take this opportunity to welcome our new Vice President, Ms. Burke Dillon. We all recognize her broad experience in development issues, and we are sure that her time in the Bank will be most productive. She will have the full support of my country.

Moving on to the economic topic, the experience of the last few years makes it clear that we are going to have to get used to living with volatility and instability in international markets. It seems a long, long time since we wrapped up the Eighth Replenishment Agreement, at a time when we were looking forward to the entrenching of the structural reforms that were under way in Latin America, with increasing emphasis on social issues.

It was within just a few months of that agreement that the first crisis broke out. While it started in one country, it ended up spreading its contagion to other economies that were solid enough, but that soon found themselves in trouble simply because market operators had a mistaken impression about them.

The crisis of 1997 spread swiftly from one country of Southeast Asia to another, but it did not really affect Latin America.

Things were very different in August 1998, when the crisis in Russia triggered the indiscriminate shut-down of debt markets for all emerging countries and provoked a generalized panic that was quite unwarranted in light of objective economic indicators.

Comparing the repercussions on Argentina from the Mexican crisis of 1995 and the Russian turmoil of 1998, we can take some comfort from the fact that the effect of the latter event has been much less severe. For example, the spread between peso and dollar bonds, which is one measure of devaluation expectations, exceeded 1,200 basis points in April 1995, whereas it was only 760 basis points at the peak in September of 1998. We can draw similar conclusions if we compare the behavior of interbank interest rates, the volume of bank deposits, or the level of international reserves.

What are the reasons for this stronger performance in 1998? The answer is fairly straightforward, and relies on three basic pillars: austerity in fiscal policy, a solid financial system, and sound management of our public debt.

Between 1996 and 1998, we reduced our fiscal deficit by more than one third, bringing it down to 1.5 percent of GDP. For 1999 we are forecasting a deficit of less than one percent of GDP.

Liquidity in the financial system, as a percentage of total deposits, rose from 12 to 30 percent between 1995 and 1998. At the same time, we consolidated the commercial banking system and moved to sell off or close down nearly all of the official provincial banks. The system was strengthened with more efficient institutional mechanisms for bolstering liquidity, such as the stand-by line for the repurchase facility that was worked out with foreign banks. This line was recently expanded, and now stands at more than US\$6.7 billion. Its operation has been strengthened with support from IDB and World Bank loans.

With respect to our external debt, we were able to extend its average maturity from 3 to 13 years between 1994 and 1998, thanks to a responsible and prudent management strategy. Our resolve to maintain control over our capacity to meet our payment obligations, even in situations of crisis, led us to extend our advance financing horizon from three to six months. Unless something unexpected happens, the new government that will take office next December will have the comfort of knowing that its first external debt payment is not due until the middle of the year 2000.

Thanks to this policy, we were able to place an issue of US\$650 million less than twenty days after Brazil's decision to float its currency, with the ensuing uncertainties that event unleashed on world markets. And since that issue we have succeeded with further ones that have brought to almost US\$2.2 billion the amount placed in the first two months of this year.

Our indicators also performed favorably in comparison with other Latin American countries during the latest crisis. I am thinking here, among other things, of the spread on Brady bonds, and the impact on domestic interest rates, as well as the pressure on the exchange rate. In fact, it is our currency board policy, which means in effect that a peso is worth a dollar, that has underpinned this differential performance, together with the other three pillars I referred to earlier. And to banish any doubt about our commitment to this exchange system, we are prepared to go further with it, examining the possibility of having Argentina adopt the dollar as its legal currency in the future. This would eliminate once and for all any lingering lack of confidence on the part of market operators, and would lead to a substantial reduction in domestic interest rates and a better overall climate for investment.

A more solid and predictable economy in Argentina will be a key factor in consolidating the integration process on which we are embarked within MERCOSUR. In the last two months, our government has given more than ample proof of its determination to proceed with building this common market, flatly rejecting pressures to return to the inefficient and protectionist policies of the past that meant only economic stagnation for our country.

Looking back on the extraordinary circumstances that Latin America has been through in recent years, and the response that has been forthcoming from the Inter-American Development Bank, I believe firmly, Mr. President, that you can be proud of the institution you lead. The IDB has shown that it has had the vision, the resolve and the leadership to provide support for Latin America in the difficult times we have had to face.

First, let me recall the prompt and effective way it responded to the fallout from the Mexican crisis of 1995, and now, the bold and sound decision to use its lending capacity to the full and to fund the emergency lending operations that were approved at the end of last year and early this year.

But the IDB has stood shoulder to shoulder with Latin America not only at times of financial turmoil, but also through the emergencies we have suffered from natural disasters. In what must surely be record time for the Bank, the Management quickly processed a loan that allowed us to bring urgent relief to areas hit by flooding in northeastern Argentina. The Bank showed the same speed again in responding to the devastation wrought by Hurricane Mitch in Central America, and to the recent earthquake in Colombia.

The year 1998 also produced an agreement on the issue of concessional resources, one that holds out new hope for the poorest countries of our region. As we said at the time, we do not find that agreement totally satisfactory, because it ends up putting the entire burden on the borrowing countries. And that burden is much heavier than was expected, in light of Hurricane Mitch and the fast-tracking of Nicaragua and Honduras into the debt reduction initiative. That is why I want to take advantage of this forum to issue an appeal to the Bank's nonborrowing members to do their part in resolving the problem—specifically, by moving up their payments on their FSO-8 contributions.

Yesterday we took a long-awaited and decisive step in the intensive efforts that have been under way to endow the Inter-American Investment Corporation with greater resources. We extend our congratulations to you, Mr. President, and to all the member countries of the Corporation for the flexibility and good will shown during the negotiations. We traveled a long road to reach this agreement, and I have no doubt that the renewed confidence we have shown in the Corporation will be amply rewarded.

In summary, we have come to the end of an intense and difficult, but productive year. Volatility, repeated crises, natural disasters—these are circumstances that surely will return in coming years. But the ability to respond that the IDB has shown in the past allows us to face the future with optimism, knowing that we will have at our side a friendly institution that is solidly equipped to fulfill the mission for which it was created.

We must continue our efforts to refine the instruments for meeting our objectives. That is why we view with great interest the work now under way in the Board of Executive Directors to draw up a corporate strategy and a human resources strategy. We also wish to urge the Bank to keep ahead of events by developing new products that will help our countries rise to the coming challenges.

I am certain that under your leadership, the Bank will continue to play a decisive role in the economic and social development of Latin America.

I would like to thank the French authorities for the hospitality they have extended to us at this annual meeting of the Inter-American Development Bank and Inter-American Investment Corporation.

The peoples and governments of Central America would like to express their gratitude to the IDB Group for the decisive support it has provided to the region through financial operations and various types of assistance for economic and social development and progress. This very positive approach was apparent in the aftermath of Hurricane Mitch. The Bank was among the first to acknowledge the devastation that had occurred, and it promptly approved various emergency operations and organized a Consultative Group made up of members of the international community. Following an emergency meeting in December 1998, the group is now preparing what is expected to be a highly productive second meeting in Stockholm at the end of May.

For some time, we have witnessed the superb efforts of the IDB Group in Latin America and the Caribbean and its capacity to generate and put into practice new ideas and to address key problems that societies in the region are attempting to solve. We therefore count on the IDB Group's active involvement in helping to resolve the major social and economic problems affecting our nations. Today, we would like to touch upon some of the issues that are of paramount importance to the countries in the region. Some of these issues are of concern to all the countries, whereas others are of interest only to the Central American nations.

Issues of Common Interest to the Region

Local Currency Conversion Program

The countries of Central America request that the arrangement approved for Honduras and Nicaragua—whereby local-currency conversion may be left to the last years of the period—be extended to the other countries adversely affected by Hurricane Mitch (i.e., Guatemala, Costa Rica, and El Salvador). This will help them through this critical period by relieving the pressures that the hurricane has caused for their export sectors.

Access to Resources

The countries of Central America welcome the initiatives taken by the IDB Group to address the current global financial turmoil by means of fast-disbursing ordinary-capital loans and emergency loans. However, they view with concern the constraints that seem to exist within the Bank with respect to the granting of ordinary-capital loans, thus placing at risk the viability of investment projects and reforms in small countries such as those in Central America. Ordinary-capital resources, including fast-disbursing funds, are essential for the region, especially in the disastrous wake of Hurricane Mitch. Central America has not escaped the effects of the international financial crises, although for the time being emergency funding has not been needed. We are concerned that some operations, such as the programs to protect our banking systems, will be subjected to the heavy costs of the emergency programs. Such a situation creates problems of equity in the distribution of Bank funds. The solution to this problem would be to "pre-allocate" available amounts so that access to ordinary-capital resources for non-emergency programs would be open mainly to small countries which are not now seeking substantial amounts of emergency resources.

Nonreimbursable Technical Cooperation Funding

When the decisions concerning the FSO were taken in December 1998, it was assumed on the basis of the information presented by the Management of the Bank that such decisions would not eliminate the funding available for nonreimbursable technical-cooperation funding in local currency and convertible currency. As this funding is extremely important for the countries of Central America, we urge Management to abide by the assumptions made in December so that we can have access to these resources in the years ahead.

Private Sector Operations

The countries of Central America would like to see a streamlining of IDB Group operations with the private sector under the Bank's private-sector window as well as with the Corporation and the MIF. The number of projects generated in the region would increase considerably if more expeditious mechanisms could be found for managing operations.

With respect to the Inter-American Investment Corporation, the Central American countries are in favor of a capital increase as well as the admission of new members. At the same time, they would like to see a strategy for all the countries affected by Hurricane Mitch—Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua; this strategy should incorporate the "Blueprint 2000: A ten-year plan for the Inter-American Investment Corporation," a document that was discussed by the Board prior to the recent natural disaster, considered by some to be the worst one to strike the region in the last hundred years.

MIF and the Environment

The countries of Central America urge Management to promote the use of the MIF to assist the private sector in adjusting to the new regulations that are emerging as a result of environmental protection programs.

I would now like to examine some specific issues of interest to individual countries.

Issues of Concern to the Countries of Central America

Costa Rica

The issue of migratory flows and their immense social impact on the economies of countries that are opening up their borders to those seeking, on economic grounds, a place to live is considered by Costa Rica to be one of the most serious problems affecting the region. The high cost that will be incurred to provide education, health care, housing, jobs, and social security for hundreds of thousands of immigrants is an issue that warrants careful study by the Bank.

The solution to the region's economic and social problems hinges on finding a solution to the problem of migration in Central America. Accordingly, we urge the Bank to look into this matter and to include it as an essential component ingredient in any analysis of the regional situation.

Costa Rica also feels that the Bank may be the appropriate forum for finding a definitive solution to the serious problem of intra regional debt. The economic well-being of the region is largely dependent on finding a lasting solution to this debt burden for both the debtor countries and their creditors.

We acknowledge with thanks Mr. Iglesias's offer to help seek a comprehensive solution to the problem and we call on him to continue his efforts along this path.

El Salvador

The Republic of El Salvador expresses its thanks to the Bank for the support received by the Central American countries, and particularly to President Iglesias for his efforts to win increased access for these countries to the markets of industrial nations. It requests that such support be maintained and strengthened in the future, and that trade continue to be one of the region's most important development issues. Also, it is grateful to the Bank for the focus placed on regional and integration projects and hopes this focus will continue. El Salvador is particularly interested in promoting a project to create a Superintendency of Central American Financial Institutions.

El Salvador hopes that the Management of the Bank will persevere in its efforts to design arrangements to solve the problem of intra-regional debt, especially debt with the Central American Bank for Economic Integration.

Guatemala

The Republic of Guatemala would like to express its gratitude for the support it has received from the Bank in implementing the peace accords, particularly the Bank's coordination of the efforts of the international community and its help in rehabilitation and reconstruction work to repair the damage caused by Hurricane Mitch. This has meant redoubling efforts to safeguard the peace accords. In this context, the Stockholm Consultative Group is viewed with optimism, not only in terms of the support that may be obtained to supplement domestic efforts but also because it offers Central America an opportunity to present the regional dimension of the process of reconstruction and transformation. Lastly, Guatemala would also like to thank the Bank for helping to find comprehensive solutions to the issue of intra-regional debt.

Honduras

With the approval of a solution to the problem of concessional resources at this critical juncture, Honduras is assured of having a flow of fresh funds for operations over the next ten years. Just as the countries showed great solidarity and ingenuity in approving this solution, the implementing mechanism will also need to be timely and flexible. Although Honduras, thanks to the support of the Bank and its member countries, is making every effort to weather this emergency phase of national reconstruction and transformation, concessional resources need to be made available as soon as possible. We therefore urge the Board to reach a decision on the local currency conversion arrangements as agreed at the meeting of the Committee of the Board of Governors in December 1998.

The availability of concessional resources will help the public sector and civil society to take appropriate action in keeping with the functioning of a modern state. However, the devastation caused by Hurricane Mitch was so extensive that the ability of the productive sectors to produce goods and services and to sustain and create new opportunities for productive employment has been severely eroded. The national effort to mobilize scarce domestic savings must receive support from the Bank's various windows for the private sector.

Nicaragua

To begin, the people and the Government of Nicaragua would like to publicly express their thanks to the countries of Latin America for the solidarity shown in reaching a consensus on the availability of resources under the Fund for Special Operations. We are well aware of the sacrifice that this represents. This once again shows the support of the borrowing members for the less developed countries. Nicaragua would also like to express its appreciation for the support being given by the nonborrowing countries so that the poorest countries in the region can move forward with the process of economic and social development. Nicaragua is grateful to the countries in the international community that opened their hearts and supported Nicaragua in the difficult times during the emergency that ensued after the hurricane, and particularly to the host of this annual meeting. Nicaragua also wishes to acknowledge the efforts made by the Bank, which responded promptly by sending missions to the country, approving operations to assist with immediate relief efforts, and organizing the Consultative Group for Reconstruction and Transformation in Central America.

Nicaragua urges the Board of Executive Directors of the Bank to implement the agreements reached on December 9, 1998, by the Committee of the Board of Governors and that it do so as soon as possible, since there is much uncertainty as to the amount of funding available for the present year. Nicaragua is concerned because it does not yet have sufficient funds to finance reconstruction six months after Hurricane Mitch, although the countries agreed to make funding available in local currency.

Nicaragua also calls on the Bank to establish and implement more rapidly a program of sufficient FSO funding for technical-cooperation projects which are essential for supporting economic development and progress in the region's poorest countries.

Lastly, Nicaragua reiterates the importance of its economic and social program being supported through more flexible mobilization of resources from the Inter-American Investment Corporation, the private-sector window, and the MIF, with a view to promoting sustainable job creation by the private sector.

To conclude, the Central American countries are very pleased with the support that the Bank has shown through its development efforts, and they hope that such support will continue on an equitable basis for the other member countries.

Introduction

It is a great pleasure for me to address the 40th Annual Meeting of the Inter-American Development Bank and the 14th 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 France and the people of Paris, for their generous hospitality.

I would also like to take this opportunity to congratulate President Iglesias for his outstanding leadership, and the Executive Directors and staff of the Bank and the Corporation, for the enormous efforts they have been making toward Latin American and Caribbean economic development.

Before going any further, please allow me to reflect for a moment on the souls of those who died in the series of unexpected natural disasters caused by El Niño, Hurricane Mitch, and the earthquake in Colombia. My deepest compassion goes to all those who suffered.

Response to the Crisis in Brazil

For two years beginning in 1996, the Latin American and Caribbean economies were on the steady track of economic growth. Last year, however, momentum for growth, I believe, has waned considerably due to a number of reasons—sluggish commodity prices, natural disasters, and the economic crisis in Brazil.

Should the crisis in Brazil continue and become more serious, the impact on the regional economy will be even greater. Stabilizing the Brazilian economy is thus of paramount importance to the recovery of growth in the Latin American and Caribbean economies.

The crises in Asia are characterized by enormous foreign capital inflows through the weak financial sector, and excessive private investments. The crisis in Brazil, on the other hand, can be attributed to the increase in fiscal deficits.

Despite such differences, however, there is something in common. In both cases, a rigid foreign exchange regime, which has allowed inflows of a large amount of foreign capital, has invited overvaluation of the local currency. There is also a more fundamental issue: in the wake of globalization of economies, emerging economies are exposed to abrupt and large-scale capital movements.

Therefore, I believe that the lessons we have learnt from our response to the Asian crises might also hold in the crisis in Brazil.

I would like to draw your attention, in particular, to the fact that in the Asian crisis countries, tightening of fiscal and monetary policies, with currency protection in mind, has gone a little too far, inviting a further contraction of the real economy. This is one of the causes of a number of problems, ranging from corporate bankruptcies to an increase in unemployment.

In Brazil, large-scale fiscal deficits have been primarily responsible for the erosion of market confidence. In this regard, it is essential for the Government of Brazil to pursue sound fiscal management under appropriate IMF programs. But, what might be learnt from the Asian experience I have just mentioned is the need to pursue balanced policy management especially in the area of monetary policy, carefully monitoring developments of the real economy.

Also, considering that the fundamental nature of these crises is that of liquidity crises, provision of adequate liquidity by the international community is necessary to prevent a future crisis, or to contain the impact should one occur. On the one hand, it is obvious that the IMF will continue to play the pivotal role in such an effort. On the other hand, I also believe that the IDB and other multilateral development banks should play an active role, too, as a crisis can jeopardize the fruits of development and will certainly affect those who live in poverty most.

In this respect, I welcome the new emergency lending program established by the IDB last year in response to the crisis in the regional countries, and the Bank's prompt response in coordination with the IMF and the World Bank.

The Issues to be Addressed by the IDB Group

There are a number of issues that need to be addressed by the IDB Group. I would like to focus on the following three.

First, poverty reduction. In the Latin American and Caribbean region today, 150 million people still live on two dollars a day or even less.

The growth of regional economies in the 1990s has not solved the poverty issue; the relative gap between the haves and the have-nots is, in fact, wider than before. What's worse, those who live in poverty have been the most apparent victims of the latest economic crisis and natural disasters.

To win the fight against poverty, an increase in per capita income through economic growth is of course essential. What's equally essential is to pay greater attention to the social aspect of development. This includes the provision of better education, better health services, and better medical care for those who live in poverty; and an improvement in the social safety net.

In this context, I highly appreciate the fact that the three-year talks among the member countries on the issue of concessional resources reached an agreement last December, thus paving the way for enhancing the IDB's capacity to address the poverty issue.

Second, the promotion of private capital inflows. Due to the crisis, private capital inflows to the region have been on the decrease. Against such a background, it is a question of vital interest to the countries in the region how they might meet the enormous demand for the capital needed to improve their economic infrastructure, the linchpin of development.

For the promotion of private capital inflows, I believe that it is essential for the IDB to make even better use of its catalytic function.

Also, for the growth of small- to medium-sized companies in the region and for the promotion of foreign capital inflows to these companies, the IIC (Inter-American Investment Corporation) can play a significant role.

In this respect, I welcome the basic agreement just reached on the general capital increase for the IIC. We must reach a final agreement at the earliest possible time, thus strengthening the financial footing of the Corporation. As for Japan, we stand ready to remain active in the negotiations to achieve an early settlement.

Third, the environment. The urban environment issue, in particular, is closely linked to poverty. As we all know, poverty in rural areas tends to invite a concentration of population in urban areas. This serves as one of the causes behind air pollution and water contamination, leading to a deteriorating urban environment. To improve that environment, it is essential to improve the urban infrastructure such as water supply and sewerage on the one hand and, on the other hand, the living standards in rural areas through rural development.

Another major environmental issue facing the region is preservation of rain forests and other forestry resources, which has direct relevance to global warming. As for myself, I believe in the motto that forestry and water control lie at the root of politics. So, I am fully aware that conservation of natural resources, such as forests and water, is of vital importance. Thus, I expect the IDB to demonstrate a strong initiative, with a pan-regional perspective.

Japan Program

Finally, I would like to touch upon the Japan Program established with our support.

With the aim of promoting exchange of experiences and policy know-how between Asia and the Latin American and Caribbean region, this program will implement research and studies on such themes as comparative analysis of the financial crises, environmental protection, the strengthening of small- to medium-sized companies and agricultural technology.

I hope that many countries in the region will take part in these research efforts and studies, so that the program can contribute to their own development.

Concluding Remarks

In closing, allow me to emphasize again that it is essential for the IDB Group to play a pivotal role in furthering social and economic progress in the Latin American and Caribbean region.

I would like to conclude by stating that Japan will continue to actively support such activities of the IDB Group.

I would like to start out by expressing thanks, on behalf of my delegation and on my own behalf, to the French Government and the City of Paris for the invitation. This meeting has been excellently prepared by President Iglesias and the Bank's Management, and I would like to thank you very much.

Latin America has made tremendous progress during the 1980s and 1990s. After years of dictatorship, democracies are again well established. Market reforms have been implemented or at least introduced. This has led to strong capital flows from abroad, resulting in above-average growth rates. While the economic success of the past years is definitely important and remarkable, we need to keep asking ourselves nonetheless to what extent it has contributed to poverty reduction in Latin America.

Yesterday I participated in the IDB Seminar "Breaking the Poverty Cycle." I am grateful to President Iglesias and the Bank's Management for the emphasis they put on poverty reduction as a central task of the IDB and for addressing the often very uneven distribution of wealth in some Latin American countries. That the Bank is a player fighting against poverty and social injustices is one important justification for Germany's membership in the IDB and the IIC.

Sadly, the development of the region has seen bitter setbacks in the past few months. Firstly, it was natural disasters that had a devastating impact in Central America. I would like to convey my sympathy in particular to the representatives of Nicaragua and Honduras, where almost all people were affected. We support the Bank's coordinating role in the aid effort and its contribution of US\$100 million for reconstruction. My government, too, showed solidarity and mobilized about US\$47 million for emergency aid and development cooperation. However, even all of this will not be sufficient. We need efforts beyond that. I will return to that point later.

The second setback was the international financial crisis spreading into Latin America. We cannot even imagine the full scope of the consequences yet. We all need to be aware that this is not only a matter of worsening economic indicators. Rather, there is the danger in the long term that millions of people will become impoverished if we do not make fundamental changes. And such change cannot be limited to the crisis countries themselves.

Development policy must not consist of unconnected parallel aid programs of individual bilateral and multinational donors. Rather, we must move towards a common global structural policy. I would like to underline three areas to describe our development policy goals:

Firstly, we want to reduce poverty and create social justice. So what we are talking about are living conditions that enable all people to lead lives in dignity.

Secondly, we want to combine economic progress with ecological sustainability. We need balanced global ecological conditions if we want to secure our common future.

Thirdly, we want to achieve respect for human rights. That is only possible on the basis of democratic principles and peaceful conflict resolution. We will make increased efforts to support these aspects, alongside with gender equality.

The guiding principle of this policy is to seek a balance of interests between, and within, the regions of the world on the one hand, and between current and future human generations on the other. In the so-called "developed" countries, we cannot continue as we have been doing. We act irresponsibly if we transfer our consumption and behavior patterns to other regions of the world.

With regard to our multi-faceted bilateral cooperation with Latin America, I would just like to mention three points: For one thing, we want to help our partners to implement sustainable social policies. That is an important contribution towards poverty reduction. The central areas of our cooperation will be education, health, strengthening socially vulnerable population groups, and land and tax reform.

Moreover, we will step up our environmental activities in Latin America. In that context, we continue to be firmly committed to the pilot program to conserve the tropical forest in the Amazon region. In addition, we are planning a climate protection program, from which Latin America, too, will benefit. The focus is on supporting renewable energies and measures to reduce CO₂ levels in the atmosphere.

Thirdly, we want to support efforts towards modernizing the State and society in Latin America. Reliable legal systems, human rights, but also modernized infrastructure and financial systems are the focal areas of our future cooperation in that field.

The current financial crisis that has taken hold of several regions of the world has shown that global problems cannot be solved without global organizations and competent regional institutions. This leads me to the topic of our cooperation with multilateral institutions such as the IDB. There are two aspects I would like to mention.

Firstly, we advocate in all the international financial institutions that structural adjustment and reform programs be designed, even more than in the past, in such a way that they are socially balanced and ecologically compatible.

In this context, I can understand that the IDB, as the largest development bank of the region, feels an obligation to contribute towards overcoming the current financial crisis in Latin America. We, too, support the decision of the Board of Governors on financial aid to Latin American newly industrialized countries. At the same time, we need to maintain the division of labor between the different

international organizations. Just like the World Bank, the IDB should concentrate mainly on its task to work for long-term development. Financial bailouts are the preserve of the IMF.

Secondly, we want to achieve a global solution for the debt problem that will be sustainable in the long term. This is why we presented the Cologne Debt Initiative, which is to benefit, not least, those Latin American countries that are particularly heavily indebted. We want to convince our partners by the next G7/G8 economic summit that the range of HIPC countries must be broadened, and debt cancellation conditions improved. Germany will also contribute to a multilateral debt fund.

However, our concern is not only solidarity between the North and the South. We should all be aware that there is also a prosperity gap between the countries of Latin America. My wish would be that the more prosperous regional member States make it possible for the IDB to make its full contribution to the HIPC Initiative.

I would like to end by stressing that I can see many aspects where the IDB's activities and the development priorities of the German government coincide. We should support each other in implementing the guiding principle of sustainability that was formulated in Rio de Janeiro in 1992. It should be the desire of all of us to attain development for Latin America that is characterized all at once by economic effectiveness, social justice, and ecological compatibility. I am looking forward to working with President Iglesias and the staff as well as with you, dear colleagues in the Board of Governors.

It is indeed a pleasure for me to be here in France and to experience the hospitality that the French government and the city of Paris are extending to us. At the same time, I thank the Management and staff of the IDB and the IIC for the preparation of our Annual Meetings.

Recalling international and regional events that marked 1998, we cannot but concede that the setting for the development of the region was not extremely good:

On one hand, the Asian crisis and then the Russian one demonstrated clearly that geographic distances do not provide protection anymore in times of international interdependence. So the financial turbulence produced shock waves that put the exchange rates, the interest rates, and the reserves in Latin America under enormous pressure. In this context, the rate of economic growth of the region suffered too.

On the other hand, in addition to this man-made turbulence, Latin America had to cope with natural disasters: El Niño, Hurricanes Georges and Mitch, and the earthquake in Colombia that brought destruction and human tragedy.

Fortunately, there was a prompt and concerted reaction by the international community — including my own country — to these disasters. Perhaps even more important was the strong and deep implementation of fiscal and monetary measures undertaken by the countries in the region.

The IDB Group itself again demonstrated its readiness and sense of flexibility. Close to its fortieth year of activities, the oldest regional development bank fought on four frontlines:

- (i) It requested and finally succeeded in getting flexibility from limits on its traditional lending to be able to join other international financial institutions assisting Latin America to overcome the negative effects of the international financial developments. We must stress that this assistance is being done in a coordinated way, that its exceptional character is clear and that regular lending is not at risk.
- (ii) The Bank spearheaded a quick and comprehensive international response to the urgent needs of the countries so heavily affected by Hurricane Mitch by organizing a Consultative Group meeting for Central America.
- (iii) It was able to finally find ways to increase the resources available for the poorest countries.
- (iv) The Bank launched the final rounds of negotiations to increase the resources of its sister organization dealing with the private sector, the Inter-American Investment Corporation. Although we do not yet know what the outcome of these final negotiations will be, we are hopeful that they will create additional financing for the corporation and allow for new members to come on board in a way that is fair to them and to current members.

Forty years after the establishment of the Inter-American Development Bank, we are able to discuss a lending program for the year 1998 that shows quite a lot of remarkable achievements:

Approvals totaled 10 billion dollars, the highest figure ever achieved. Even if we exclude the emergency lending of 2.8 billion dollars, there is still an outstanding figure for the regular program of 7.2 billion dollars.

Even more important to us is the fact that 46 percent—nearly half of all lending—was devoted to the social sectors, thereby affirming where this institution's main focus lies.

Although once again the 35 percent lending target in favor of the smallest and poorest countries was not met, at least 30 percent of lending was granted for these groups.

I should also add here that we are concerned that the new classification system could negatively affect the smaller, poor C and D countries.

We are pleased to note that around 87 percent of regular loans were investment loans.

We particularly appreciate the fact that lending from the Fund for Special Operations has more than doubled in the past year.

But the good news are not restricted to the Bank: despite all the constraints on its financing, lending by the Corporation in the past year shows a significant increase compared to the previous year, and close to half of all resources went to the poorer countries of Groups C and D.

I would now like to turn to our expectations for the future of the Bank.

On content, we expect the IDB to remain in a financial situation that will allow it to consider short-term emergency activities from time to time, as might be necessary given possible future developments. But even when responding to short-term emergency needs, we—as shareholder—and the Bank must not neglect the long-term developmental responsibility of the Inter-American Development Bank. This leads me to the subject of poverty reduction. Economic inequalities have increased and unemployment has risen despite economic growth. If not dealt with adequately, these developments could lead to growing tensions, political instability, and social unrest. As

economic growth and liberalization alone cannot solve Latin America's problems, we support the IDB's continuous efforts to work closely with the governments and with all sectors of civil society to ensure that these problems are resolved and economic wealth is distributed more equitably. In this connection, I would like to congratulate the Bank for its 1998-99 report, *Facing up to Inequality in Latin America*, examining why the societies of the region are so unequal and suggesting what can be done about it.

On procedure, we expect the multilateral character of the institution to be fully respected through timely integration of all the countries in the decision-making process for all kinds of important issues.

This meeting, commemorating the fortieth anniversary of the founding of the Inter-American Development Bank, provides me the opportunity to extend to the French people and to our host city, Paris, the cultural and intellectual birthplace of our age, a heartfelt greeting from the people and the government of Ecuador.

I would also like to express my particular admiration to you, President Iglesias, for your tireless support of causes that are of concern to all our countries. The catalytic role that you play in securing a prosperous Latin America inspires us to persevere in our efforts. I should also like to extend my best wishes to Ms. Burke Dillon in carrying out her new functions as Executive Vice President of the institution.

In the following remarks, I would like to highlight the main events in Ecuador which I believe it is important to bring to the attention of the Governors at this meeting.

Doubtless the most significant among these, in 1998, was the signing of the peace agreement with Peru, which put an end to more than 180 years of conflicts, the only result of which was to destroy opportunities for the integration and development of our peoples.

The joint decisions and efforts of President Fujimori and President Mahuad brought an end to this long chapter in our history, making it possible to approach the future with a spirit of hope and fraternity between two neighboring peoples.

Achieving this long-sought peace was a first step in the agenda which the new Ecuadorian government defined when it came to power last August. Having accomplished this, we are making concerted efforts to find solutions to the grave economic and social crisis that our country is experiencing.

The effect on our economy of El Niño and the decline in the price of oil were reflected dramatically in the area of public finance, increasing both the fiscal deficit and the trade deficit.

To cite one statistic, of the US\$678 million which Ecuador expected to receive in 1998 from oil exports, it received only US\$222 million, representing a drop of US\$455 million, equivalent to 2.5 percent of this year's gross domestic product.

In terms of the impact of El Niño, the losses both in physical capital and in revenue flows are enormous. According to figures provided by ECLAC, direct costs from El Niño are the equivalent of four percent of GDP, while indirect costs to the economy represent 10.6 percent of GDP.

In addition to this, extreme volatility in the international financial markets resulting from the Asian and Russian crises led to a considerable reduction in the flow of financial resources needed to cover the deficit, which to a great extent was caused by the shocks to our economy.

One of the most significant among the actions and challenges that the Ecuadorian government has had to deal with in its first eight months was the effort to consolidate constitutional order. We are the heirs to two successive 'nongovernments' which were the authors of the economic disorder we face today, and which could create fertile ground for demagoguery and political opportunism.

Because of this, the most difficult challenge has been in the political, rather than the economic arena, and consequently we have at times had to give precedence to political solutions over technical considerations.

There are political problems to which Ecuador must find solutions. At the center of diagnosing, making proposals for, and implementing economic measures, is the issue of exercising and consolidating democracy.

Nevertheless, much remains to be accomplished in order to correct the structural problems that are the cause of the imbalances we face.

The determination to correct the distortions which, internally, continue to affect the price of certain basic services, led the government to implement a set of reforms that will attack the root cause of the pressing fiscal problem.

The elimination of a series of general subsidies, along with the significant reduction in public sector spending, were the first tools used to deal with the problem, making it possible to send to the Congress the draft budget for 1999 in line with the realities of the country and the situation in the international markets.

However, the situation that has developed in recent weeks has required the national government to take even more radical measures than those envisioned when the draft budget was sent to the Congress.

In the past days, the President has announced a set of fiscal, as well as banking measures to correct the problems caused by the heightened sense of anxiety our economy has experienced; temporary measures, the purpose of which is to protect the public's deposits and ensure that banking operations are normalized in a way that does not affect those institutions that fall within the required parameters for solvency and security.

Particularly important among the main points of such a program are: sending to the Congress a plan to increase the value added tax from 10 percent to 15 percent; eliminating a series of VAT exemptions, preserving only those related to food and medicine; and establishing a tax on luxury vehicles.

The government intends, in the very near future, to enhance fiscal revenue through a comprehensive reform of the tax system which will provide the budget with a permanent means of support and eliminate chronic deficits.

Pending the approval of these reforms by the national congress, the price of fuel has been increased, allowing the State to have immediate access to the funding needed for dealing with the crisis.

This made it necessary, however, to define more efficient instruments to serve the poor segments of the population in a targeted way, since they are more seriously affected by the adjustment.

To this end, the Government designed a compensation system, through the provision of a "solidarity allowance" intended for the most vulnerable population. This has been increased by 50 percent to mitigate the effect which the most recently adopted set of measures will have on its value. It should be mentioned that at present the "solidarity allowance" is provided to more than 1.6 million people throughout the country.

At the same time, the Government's efforts have been aimed at ensuring the highest possible level of funding for the social sectors, given the restrictions under which the country is operating. Improving equity in the sectors of education, health care, employment and social welfare is central to the social agenda which the Government has defined to alleviate the poverty of the majority of the country's population.

These objectives are, without doubt, fundamental and thus require commitment and resolve not only on the part of the national government and the country as a whole, but also on the part of organizations such as the Inter-American Development Bank which, through its support, has made it possible to define actions precisely along these lines.

Projects recently approved for education and emergency assistance related to El Niño, along with the encouragement given to operations currently being implemented in the areas of housing, child care and the Social Investment Fund provide us with resources to appropriately meet these objectives.

The actions which have been instituted in relation to the financial sector are aimed at eliminating the sense of anxiety and the speculation which have strongly affected our economy in recent weeks. A scheme for the rescheduling of assets and liabilities has been established, bringing order to the system until the necessary corrective regulatory and operational measures are taken, providing the country with a solid and lasting sector which contributes to the consolidation of the country's economic development.

The actions just mentioned require urgent support for Ecuador by the international community. I would therefore like to renew my country's request that the Inter-American Development Bank, together with other multilateral institutions, participate in a joint financing program which would assist us in dealing with the difficult crisis we are experiencing.

We must not jeopardize our democracy and, above all, we must not endanger the future of our people. At present, Ecuador is like a patient on the operating table, in critical condition. If we allow this chance to slip away, it could provoke an irreversible process that would bring much greater suffering to the most fragile segments of society, as well as providing an unfortunate message about the region to the markets.

Next, I would like to discuss what I consider to be the most important elements of the activities carried out by the Bank and the Corporation during the past year.

The first of these, certainly, is related to the agreement on concessional resources. This agreement was reached primarily as a result of the determined participation of the Bank's borrowing countries, which have permitted the conversion of most of our local-currency holdings in the Fund for Special Operations.

However, this effort should also serve as a call to our nonborrowing members which, without minimizing the commitment they have shown in previous years to the institution as an instrument for development in Latin America and the Caribbean, must now look to the future as an opportunity to ratify this commitment by providing additional resources beyond those involved in the conversion. This is required by the current needs, which continue to exceed the available resources, as shown by the levels of poverty which persist in all the countries of the region.

There is also little doubt that one of the features of the IDB during its forty years of existence has been its ability to assist countries in the design and implementation of policies, project execution, and the dissemination of knowledge on topics such as integration and education, through its technical cooperation program and through other means.

I would urge the Bank to assure that all necessary resources are made available to continue the activities related to this facility, which certainly differentiate it from traditional sources of financing serving the region.

Another important element in the Bank's management this year has been its role, in conjunction with other institutions, in meeting the requests of countries in the region for dealing with the needs arising from the crisis in the financial markets. On this point,

we should recognize the importance of acting in a timely way on joint actions on the part of organizations whose function is to foster the consolidation of economic development, in the broadest sense of the word.

The experience we have gained in the region in dealing with the crisis—for some, the result of contagion, for others the result of structural problems in our economies—emphasizes the role which all the multilateral financial institutions have had, and in particular, the role of the Inter-American Development Bank, which we feel is intimately connected with the reality of our countries.

I therefore wish to repeat the request that this effort be extended to all countries in need, given that the markets regard us as a region, rather than individually. Thus, preventing a worsening of the crisis for some helps prevent contagion to all.

I would also like to express my support for the work of the Bank in fostering activities by the private sector in Latin America and the Caribbean. We remain convinced that this instrument is of paramount importance in strengthening the physical infrastructure that supports the growth of our economies, and urge that every effort be made to serve more countries of the region as soon as possible with resources from this facility.

These days have also served as a framework for the negotiations that resulted in the capital increase of the Inter-American Investment Corporation. As I indicated previously, Ecuador has full confidence in the efforts of the IDB Group in encouraging private sector participation in the region's development, and in particular, the role that small and medium-sized enterprises, as the main recipients of Corporation assistance, play in this process.

We therefore welcome this increase and once again express our interest in seeing a Corporation renewed in its drive to serve the region. The efforts which the member countries are going to make to capitalize the Corporation should go hand in hand with an appropriate level of profitability which at least makes it possible to maintain the real value of the capital contributed and, most importantly, makes it possible for the Corporation to reach, to one degree or another, the sectors for which its creation was intended.

Finally, I would like to once again express the desire of the Ecuadorian government to see the Inter-American Development Bank in the forefront of efforts to secure an integrated, vigorous, and democratic Latin America in which poverty and violence have been eradicated and where the future reflects the united work of all of our peoples.

Let me start by thanking the French authorities and the city of Paris for hosting this year's Annual Meeting of the IDB and IIC. I hope that this year's Meeting will be as successful for the IDB-Group as last year's World Soccer Championships were for the host country. As you will surely understand, I do not wish to dwell on that subject for much longer.

The Financial Crisis and Implications for the IDB

On a more serious note, the events which really shaped 1998 were of a very different character. It was a year of turmoil in international financial markets. Many countries witnessed an increase in their costs for international borrowings. Financial flows were excessively volatile. Still, it is noteworthy that not all countries were equally affected. Clearly, countries with better fundamentals were hurt less by contagion. The IDB-Group has an important role in assisting countries in structural reforms that contribute to sound fundamentals, including a well functioning financial sector. It is better to consult your doctor before you get ill. Of course, it is even better to live healthy.

Unfortunately, nature has not treated the region well either. We would like to express our feelings of empathy with the numerous people who suffered from natural disasters. The President and Management deserve credit for their timely interventions, in particular with respect to addressing the consequences of Hurricane Mitch.

Concessional Resources

On the IDB itself, 1998 was a year in which significant decisions were taken. We very much welcome the agreement on concessional resources. The solidarity shown by borrowing member countries was an important element in this respect. The agreement will safeguard the continued provision of concessional resources to the poorest countries in the region.

However, there is still one loose end: the financing of HIPC-debt relief for certain countries. The Netherlands is the largest bilateral donor to the HIPC-Trust Fund. This illustrates the importance we attach to the HIPC-initiative. The IDB's contribution is necessary to enable the eligible heavily indebted countries, including the ones hit by Hurricane Mitch, to benefit. As a direct consequence of the decision not to use OC net income to fund the HIPC contribution, sufficient FSO-resources need to be set aside for this purpose. In resolving the outstanding issues, we hope that solidarity will again be a leading motive.

IIC Capital Increase

On the issue of the development of the private sector, the Netherlands favours a policy where the IDB remains focussed on creating an enabling environment. Fortunately, the IDB-Group has the IIC and the MIF as specialised instruments for direct investment activities. In this connection, I am very pleased with the consensus on a capital increase for the IIC. I hope that both founding members and potential new members will find the wisdom to settle the remaining outstanding issues as soon as possible and in a spirit in which individual countries' ambitions do not prevail over the overall interest of a speedy implementation of the capital increase. In this regard we very much support a further discussion on IIC operational policies.

Corporate Strategy

Turning again to the IDB, we very much welcome the Corporate Strategy process. Before commenting on it I would like to say a few words about a recent change in the Dutch development assistance policy. From now on, the Dutch assistance will be redirected towards fewer countries. The selection of countries is based on three criteria: 1. the poverty rate and need for assistance, 2. the quality of social-economic policies, and 3. good governance. At the same time we will enhance our co-financing with multilateral channels. We will strengthen the sectoral focus in our programs rather than providing aid on a stand-alone project basis.

Coming back to the Corporate Strategy process, we hope that the IDB can also put more emphasis on a sectoral approach. Adequate co-ordination with other multilateral and bilateral donors in each country has to be part of this approach. I am glad to note that also the World Bank is thinking in this direction. The key is co-operation on equal footing and the avoidance of overlap and competition. These principles should also apply in relation to the IMF's activities.

Emergency Loans

This explains our sceptical stance on the concept of IDB-emergency loans. Liquidity support in times of crisis and associated macro-economic focus are the primary responsibility of the IMF. We understand that in last year's turmoil, the IDB felt the need to assist major shareholders in times of need. But, we have to be aware that there is no free lunch. IDB's headroom has disappeared. This is already jeopardising the Bank's regular program. This is clearly undesirable and unsustainable. The Bank's resources should remain available for complementary structural reforms.

The IDB-Group has built an impressive track record over the past forty years. We congratulate management and staff on the Bank's achievements. For the future, the IDB has to focus on its core mission. It should continue to direct its attention at poverty alleviation and the promotion of economic and social development. In doing so, country and sectoral strategies will have to play a larger role. The Bank should not aim to be everywhere on the playing field of development. This is where the Bank can learn from soccer-players. Even players like Ronaldo and Batistuta cannot be everywhere on the field and still score goals. They are most effective when they direct their attention to what they are best at. Mr. Chairman, Mr. President, fellow Governors, Ladies and Gentlemen, the same applies to the IDB.

I take great pleasure in speaking today on behalf of the Caribbean Constituency in the Inter-American Development Bank, and the Inter-American Investment Corporation. The Constituency comprises The Bahamas, Barbados, Jamaica and Trinidad and Tobago, as well as my own country, Guyana. I wish to join my colleagues who have expressed sincere appreciation to the Government of France, and particularly to the Mayor and the people of Paris, for their generous hospitality; and the excellent arrangements for this Annual General Meeting.

We wish to welcome Ms. Burke Dillon, our new Executive Vice President, who has joined our Bank at a very critical period of its life, and we look forward to her contribution to its future progress. At the same time, we place on record our appreciation of the role that her predecessor, Ms. Nancy Birdsall, performed, and extend to her our best wishes for success in her future endeavors.

The year 1998 will be remembered as one in which Latin America and the Caribbean experienced the severe effects of both international financial crisis and natural disasters of unprecedented proportions. Indeed, 1999 began with financial difficulties persisting in the region and a major earthquake in Colombia. This followed the earlier hurricane disasters experienced by the Caribbean and Central America. We extend our sincere sympathy to the governments and people of all the affected countries. The Bank has been prompt to implement emergency financing, and organise adjustment programmes for these countries, in close coordination with other multilateral agencies. We applaud the Bank's efforts to strengthen our countries' capacity to withstand global turbulence and natural disasters and protect their hard-won progress in the present decade. Despite the evidence that global financial volatility has begun to abate, our institution must remain alert and flexible in order to provide appropriate support where necessary.

In Latin America and the Caribbean, as a result of the financial emergency and the effects of natural disasters, the real GDP growth rate fell from 5.3 percent in 1997 to an estimated 2.7 percent in 1998. These developments make more important the role that the Bank must continue to play in our Region, especially in order to restore it to its previous higher growth performance.

Performance of the Caribbean Economies

The major factors that affected the performance of the Caribbean economies in 1998 were the impact of El Niño in Guyana and other adverse weather conditions elsewhere and declining commodity prices in the sub-region as a whole. Guyana recorded negative growth, resulting from a fall in agricultural output and a decline in prices of major export commodities. Jamaica's output continued to be constrained. The Bahamas, Barbados, and Trinidad and Tobago achieved rates of growth which were not significantly lower than in 1997. In The Bahamas and Barbados, growth came mainly from the tourism and construction sectors, while in Trinidad and Tobago the effects of the oil price decline were mitigated by large natural gas-related investment. Inflation continued its downward trend, with Barbados recording negative inflation, after having fully absorbed the impact of the implementation of the value-added tax in 1997.

IDB, IIC and MIF Activities in Support of the Caribbean Economies

The Annual Meetings provide Governors with a welcome opportunity to examine the vital role that the IDB group of institutions performs in assisting the development of its borrowing members. Our Constituency believes that these occasions can be used to identify areas in which the contributions of the Bank, the Corporation, and the Multilateral Investment Fund could be improved. From this perspective we would note that the recent performance of the Bank Group has not met our expectations, particularly since the level and regularity of approvals and commitments continue to fall short of our needs. Although total commitments of \$132 million in 1998, distributed among five projects, were almost double the amount received in 1997, these approvals— as in the previous year— were obtained for only three of the five members of our Constituency. This situation may stem from a process which overloads projects with conditionalities that delay preparation, and hinder prompt and effective implementation. Loan disbursements to our Constituency in 1998, amounting to \$161.7 million, were slightly lower than in 1997. At the same time, a matter of great concern to us is the outflow of resources from our countries to the Bank resulting from the high level of ongoing loan service charges.

As the major source of development assistance for our countries, it is imperative there be sustained efforts to improve the quality of the programming dialogue between the Bank and our members and the efficiency of project development and execution. We believe that this could help resolve existing problems of Bank procedures that are too slow and protracted. The C & D Action Programme has helped to relieve some of the problems and we urge that it be continued beyond 1999. We need to ensure a net inflow of resources from the Bank through urgent and sustained improvement in all aspects of the project cycle, and we call on the Bank to renew its support for this objective.

The IDB-8 Guidelines assign an important role to the private sector in the development of the economies of the Region. The Private Sector Department, the Corporation, and the MIF are specifically charged to support that objective. However, in our Constituency, their efforts need to be strengthened and sustained to produce tangible results, which, prior to now, have been scant at best.

We must commend the Committee of the Board of Governors for proposing a solution for augmenting the FSO convertible currency resources to provide for the regular needs and the more recent disaster-related requirements of the poorest members of the Bank. However, while the recently approved resolution represents a pragmatic attempt to provide concessional resources to the members of the Bank that are in greatest need, it fell far short of the equitable burden-sharing arrangement in which all members should contribute. We support the Committee's emphasis on adopting a long-range perspective, for all the foreseeable contingencies, under which FSO financing may be required, including the provision of debt relief under HIPC programmes for Nicaragua, and Honduras.

Repositioning the Caribbean in the Bank's Activities

Last year, in our statement to the Thirty-ninth Annual Meeting of the Board of Governors our Constituency presented an Agenda for Bank action to support the development process in the Caribbean countries. That agenda focused on areas such as the promotion of export led growth within the context of efforts to achieve a greater integration of our resources and domestic markets; the elimination of poverty and the removal of social inequality; and the protection and improvement of our natural environment. These areas of activity are squarely within the GRI-8 mandate. We wish to record our appreciation for the support that the Bank has provided for our effort to improve our trading access through its contribution to the financing of the Regional Negotiating Machinery. We also appreciate the proposed assistance for CARICOM as indicated in the Regional Programming Paper on the Caribbean Community. We hope that these efforts will be sustained by adequate financial provisions.

At our Annual Meeting in Cartagena, we began a process of reviewing our fulfillment of our Eighth Replenishment guidelines. Our Executive Directors, the Management, and the senior staff of the Bank have been devoting considerable attention to re-examining our objectives, and the instruments, procedures and methodology for achieving them. We believe that Governors support this work, and should await specific recommendation to emerge rather than attempt piecemeal adjustments to various aspects of the governance of the Bank.

It is in this context we must register our concern that the GRI-8 mandate that requires the Bank to seek to allocate 35% of its annual lending program to the C and D members of the Bank has been altered to remove three of the five members of our Constituency—Bahamas, Barbados and Trinidad and Tobago— from its coverage. We need to receive assurance from the Bank that it is not proposing to abandon its well-established principles of providing a commensurate level of assistance to the smaller members of our Institution. We would urge the Bank to join the efforts of other members of the multilateral community who are seeking to develop measures other than per capita income to assess the capacity for socio-economic transformation of small vulnerable economies, and provide them with appropriate support.

The Caribbean constituency recognises the reality of the financial crisis facing the Latin American economies arising from massive capital flight and the rapid drying up of normal access to private markets. We are particularly conscious of the effect of contagion from other parts of the world on our Hemisphere. We understand only too well the onerous implications of this situation for social and economic welfare for the region as a whole. As small open economies, we in the Caribbean have a strong vested interest in the avoidance of systemic disruption in our region and in the wider world. We shall continue, therefore, to support the Bank in its search for balanced and well conceived measures to counter unfavourable developments in other areas of the Hemisphere even as we look to the renewal of its efforts in our own.

Our strategic focus must remain fixed on the promotion of development, through the elimination of poverty and inequality in our Hemisphere, that has been the initial objective of our Bank, and remains its essential mission. It is important that we find ways of ensuring that this core objective remains our fundamental purpose, even as we deal with unexpected economic disruptions as we have done in the past year. Let us make this meeting the occasion for renewal of our commitment to the goal of integral development in our Region.

I should like to thank the French Government for hosting this Annual Meeting of Governors in this lovely city—Paris—and to thank the Bank for the arrangements they have made for this meeting.

At last year's Annual Meeting in Cartagena, we were looking forward to celebrating the Bank's fortieth birthday, and rejoicing in the way that the financial crisis in Asia seemed to be having little impact on the countries of Latin America. But as the crisis spread to Russia, the shock waves have also been felt in Latin America. Access to external finance was reduced; exchange rates declined, interest rates rose and growth rates fell.

As if that were not bad enough, there were a series of natural disasters too—El Niño, Hurricanes Georges and Mitch, and the Colombian earthquake.

All of this has shown the extent to which there is a role for the IDB to play, aside from its normal lending operations. It is appropriate that, in exceptional circumstances, in responding to the financial crisis, the IDB should contribute to emergency lending programmes, as part of international packages of support. We recognise the importance of such loans to Brazil, Argentina and Colombia.

We welcome the close relationship that has developed between the IMF, World Bank and the IDB in crisis countries. While the IMF provides liquidity support, there is much for the development banks to do in helping with structural reform to prevent a reoccurrence of such crises. In accordance with their developmental mandates, they should focus on structural and social issues, helping to minimise the effects of the crisis on poor and vulnerable groups.

In February, my colleague Clare Short, the Secretary of State for International Development, co-hosted a very successful seminar in London with President Iglesias on the Bank's report on Facing up to Inequality in Latin America. Yesterday, I chaired a session of another seminar on this vital topic. We very much welcome the Bank's important contribution to identifying why, given its stage of development, Latin America should be the most unequal region in the world. Increasingly, it is recognised that inequality constrains growth, sustainable development and poverty reduction. It is unacceptable that, despite the economic and political reforms in the region, nearly half the population of Latin America have received no benefit. Inequality—coupled with poverty, unemployment and social exclusion—remains a major problem. Appropriate economic reforms must be complemented by social reforms to ensure access of the poorest people in the region to basic health care and education.

The fight against poverty and inequality must therefore remain firmly at the centre of the Bank's work. It is essential to ensure that all—no matter what their race, colour, creed, gender or class—benefit from the opportunities being created. It is important that assistance is focused on some of the biggest excluded groups: for example, the indigenous populations and black minorities where there are large concentrations of poverty. If we do not make progress, inequality, instability and environmental degradation will only get worse instead of better. This is unacceptable as we move towards the new millennium and I hope the Management of the Bank will do more in the coming years to turn fine words into real action.

Continuing inequality is a divisive force. It is important to convince the elite of Latin America that it is in their interest too to secure change. We must form a new consensus about how to achieve more rapid reduction in poverty and inequality. Governments, the IDB, donors—bilateral and multilateral—civil society and the private sector need to work together on this.

The Bank is playing an invaluable role in co-ordinating responses to the reconstruction of Central America following the devastation caused by Hurricane Mitch. Like others here, the UK is contributing to this effort which was brought home to us so vividly through television pictures. Our Chancellor of the Exchequer and Secretary of State for International Development proposed the establishment of a Trust Fund for Honduras and Nicaragua to help them meet their debt service payments to international financial institutions. Having contributed \$16million ourselves to this, we are pleased that total commitments now exceed \$100 million.

Efforts to eradicate poverty are constrained by the level of debt owed by some poor countries. We are strong supporters of the Heavily Indebted Poor Countries (HIPC) Initiative, but recognise that debt service payments are still too high in the early years. There are doubts, too, whether, as intended, countries are achieving a sustainable exit from their debt problems. Recognising that faster and deeper debt relief is therefore required, the UK Government pressed successfully for a fundamental review of the HIPC process. We have also challenged our creditor partners to agree to cancelling \$50 billion of debt by the end of 2000 for those countries whose governments are genuinely committed to eradicating poverty. To bring this about will require a special effort by all creditors—multilaterals and bilaterals.

But debt relief is only worth doing if it releases money to spend on services which help the poor. In the fight to eliminate poverty, we recognise the unique contribution which the multilateral development banks can make through the scale of their resources and the influence they can bring to bear.

Last year, I urged the Bank to adopt the International Development Goals, which are the culmination of a series of landmark UN conferences and meetings in the 1990s and, most importantly, are endorsed by all member States of the UN, both developing and developed countries, many of whom are also members of the IDB. The targets include halving by 2015 the proportion of the world's population living in extreme poverty as well as specific targets for universal primary education, reductions in infant and maternal mortality

and environmental degradation. Progress towards the goal of eliminating poverty in poorer countries can be measured against them. The World Bank and the African Development Bank have already committed themselves to the targets, and I ask now that the IDB do so, too—integrating them into its country strategies.

It is clear that some countries will continue to need concessional resources in the coming years if they are to address the needs of the poor. We are therefore pleased that, following lengthy negotiations, agreement has been reached on providing additional resources for concessional lending. I should like to thank the Board of Executive Directors and its Working Group on Concessional Resources for their hard work on finding a solution to this issue. I also applaud the solidarity shown by borrowing countries which have agreed to the conversion of FSO local currency resources. I recognise that this has not been easy. It is welcome that, as part of the agreement, the IDB has reaffirmed its commitment to poverty reduction in the Western Hemisphere and, in particular, in the poorest countries of the region.

In its 40 years of existence, the IDB has always held its annual meetings in truly exceptional cities. Whether in Europe, Asia, or the Americas, the host cities have invariably stood out because of their personality or their history, their natural setting, or their architectural beauty. Today we are privileged to meet in a city that has personality, history, and natural and architectural beauty, in other words, the attractions of all the others we have visited combined.

Once again the Bank Group comes together at its annual meeting with an outstanding performance to report for the year. However, unlike previous years, this time its performance was achieved in a context that was extremely difficult and complex economically, and to some degree politically as well. After the somewhat far-off Asian turbulence that was already a concern when we met in Cartagena, 1998 brought the Russian crisis and, beginning in September, the financial difficulties that shook our region to its very core.

Within the space of just a year, these major outbreaks of financial uncertainty appeared and confidence in emerging markets continued to falter, thereby leading to higher costs and a relative downturn in financial inflows to the region. This context of instability can lead to difficulties in the current systems of international financing. If investor mistrust and volatility in international capital flows were to persist, the growth of our countries would be seriously compromised.

In Uruguay, the policy of phased structural reforms has been maintained and implemented in such a way as to ensure continued economic and social stability and sustained growth, while at the same time effectively protecting the country against international turbulence.

The key to maintaining confidence has been the strict fiscal discipline instituted by the coalition government. In 1998, the fiscal deficit, including the high cost of structural reforms in areas such as the social security system, amounted to 1% of GDP. Economic growth was 5.3% in 1996, remained stable at 5.1% in 1997, and was 4.5% in 1998. This performance meant an average annual increase in per capita GDP of over 4% during that three-year period.

Inflation continued its downward trend during the period falling to 8.6% by year-end 1998.

Salaries and real income for families continued to grow at a slow but steady pace. Unemployment has remained at about 10% for one year, although unfortunately a slight upward trend is apparent.

The forecast for 1999 indicates a period of a slowdown in growth, perhaps even a contraction in economic activity. Under the circumstances, it is essential that the current reforms be deepened in order to improve the competitiveness of the economy and preserve basic economic equilibria, since this approach has proven the best course to navigate the recent financial storms.

The Bank, in this new context, has responded rapidly and judiciously to the risks generated by the sudden fluctuations in the financial markets in the countries of the region.

An essential element in the Bank's response to the harsher financial environment has been greater coordination of its activities with the International Monetary Fund and the World Bank.

However, if this economic trend persists, the IDB can be expected in the short term to become one of the few easily accessible sources of financing for many countries in the region. We must therefore consider whether institutional mechanisms should be created to mitigate the impact of international financial volatility. Moreover, in our opinion, multilateral financial institutions must make every effort to support inflows of external resources into all our countries.

This is particularly important for Uruguay.

This new situation of a "relative lack of resources" led the IDB to set a number of criteria for the allocation of the increasingly scarce funds available. In the long term, these constraints may prove relatively unfavorable for a small country like ours, which is among the more developed ones in the region.

For the less developed countries, the Bank has been able to reach an agreement through a sort of reformulation of the system for financing the Fund for Special Operations that will ensure that the financing needs of the poorest countries in the region can be met for a prudent period of time.

When the financial emergency arose in certain larger countries, the Bank swiftly approved a series of emergency mechanisms to ensure the stability of their economies.

These two approaches to the harsher international financial environment seem appropriate to mitigate the attendant risks of this new situation and to contain possible contagion of financial instability elsewhere in the region.

However, we would like to point out that to a greater or lesser extent all the economies of Latin America and the Caribbean will have to endure some adverse impact from the current situation. The Bank should therefore make sure that these recent decisions, basically targeting the largest economies and the least developed countries in the region, do not ultimately compete strongly with the regular financing needs of small and mid-sized countries at an intermediate level of development.

Certain troubling symptoms of this problem can be perceived in the access to new fast-disbursing sector loans for countries that have not declared a "financial emergency" and with respect to technical cooperation, an issue that our country has repeatedly raised for years during previous annual meetings.

Nevertheless, with regard to the activities of the Multilateral Investment Fund, we are pleased to point out that support for our countries has not declined. The trend towards a higher level of activity—a trend we had noted two years ago—seems to have been consolidated. The programming process for MIF operations has not only itself improved but in addition is now much better coordinated with the programming process of the IDB Group as a whole.

As for the Inter-American Investment Corporation, it should be noted that we have reached an agreement of major import that will lead to effective capitalization of the Corporation. This will be achieved through fresh capital contributions by the member countries of the Corporation but also as a result of the determined efforts made by the Management and staff of the Corporation to modernize its organization and thus be in a position to fulfill more efficiently its mandate of supporting small and medium-sized enterprises in the region. With a US\$500 million capital increase, in our view, the Corporation will become a powerful instrument for the development of small business in the region's private sector.

Given all these achievements, I cannot conclude without conveying the sincere appreciation of the government of my country to President Iglesias and the entire staff of the Bank for the many contributions they have made in the past year to the successful implementation of our joint projects in Uruguay.

It gives me great pleasure to address this meeting of the Governors of the Inter-American Development Bank. On behalf of Canada, I want to thank our hosts, the Government of France, for welcoming us to this incomparable city.

Canada sees the IDB as a key development institution of the western hemisphere. We count on it for vigorous leadership so that all the people of the Americas can achieve high levels of social, economic and political well-being. We strongly support the Bank's mandate, and its work—and we will continue to play our role, as a regional member, with enthusiasm in the 21st century.

Regional integration offers the Americas our best path to a future of human security, economic prosperity, and social justice. Beyond the Bank's own particular operations, it is contributing to the region's progress by playing a valuable, even unique, supporting role in many aspects of integration and hemispheric cooperation.

In recent years, the Summit of the Americas process has given new drive to the development of a true hemispheric agenda. At Miami and Santiago, our democratically elected leaders endorsed ambitious plans of action. These plans, in areas ranging from human rights to free trade, aim at raising the quality of life of all the people of the Americas.

Canada is proud to have been a leader in this process, and an active participant in the intense round of follow-up work. We commend the Bank for its support, as coordinator for various themes, of the Summit process. But we can all do more—and we urge the IDB to use its resources even more actively to support the whole range of mandates endorsed by the leaders. We believe the Bank should also play an even larger role in meeting the priorities agreed to by the member States of the OAS. It should, in short, become central to carrying out the agenda of the Americas.

An urgent part of that agenda is, clearly, the issue of human security. We face concerns and challenges that affect all of us, and we need to create new partnerships and find fresh approaches. One threat alone—illicit drugs—causes violence and crime, distorts economies, deepens inequity, and undermines human rights and democracy. The governments and people of the Americas must and can work together to overcome such grave challenges.

We are also encouraged by the growing cooperation we have seen among the hemisphere's institutions. Collaboration between member countries and regional institutions in the Tripartite Committee with the OAS, and in the UN Economic Committee for Latin America and the Caribbean, is clearly helping to solidify this spirit of solidarity. While challenges still lie ahead, we believe the negotiations for the Free Trade Area of the Americas are on track... and we look forward to a productive Ministerial meeting in Toronto this coming November.

Increasingly, the Bank finds itself working along with other multilateral organizations to finance various programs. We encourage such deepened cooperation—but we sense that, particularly in the areas of governance and policy-based lending, the field is sometimes crowded... so a harder look at the core mandate and the comparative advantage of institutions, including the IDB, would be wise.

The Free Trade Area of the Americas is being built, step by step, in a spirit of solidarity. As Chair of the Trade Negotiations Committee, under the FTAA process, Canada is very pleased with the progress made to date, especially in the area of business facilitation.

Achievements and Challenges

Emergencies—natural and financial—battered the region in 1998, testing the ability of all to respond.

Canada is keenly aware of the tragic impact of natural disasters, most recently Hurricane Mitch. Indeed, we have taken special steps, such as providing debt relief for the hardest-hit countries, and pledging additional aid for Central America, which Prime Minister Chrétien will soon be visiting.

The Bank is helping to tackle these new needs—reconstruction in Central America, financial volatility impacting on the large regional countries—while still delivering on its core mandate of social and economic progress. So we applaud the Bank's impressive initiatives last year to support recovery from natural disasters, and to maintain financial stability in Latin America's biggest economies.

Despite the trials and setbacks of the past year, the region's long-term prospects are bright. Its economic foundations are in good shape. The fundamentals for growth are strong in many countries. Reforms are being carried out region-wide. By adding investment in education, social development, effective governance, and addressing inequality head-on, the Bank can effectively meet its mandate, and the region can achieve its destiny.

For both the Bank and its region, 1998 was a year of promising achievements, as well as new or continuing challenges. Loan approvals and disbursements hit record levels—further evidence of the IDB's relevance to its members' needs.

And yet, at the end of the day, the Bank's success, its relevance, its legitimacy, will depend on its developmental impact—especially on the number of poor it has helped to build better lives. This is the Bank's true role. This must always be priority number one.

Thus, while we recognize the pressing needs of the larger member countries for fast-disbursing 'line-of-defence' financing, we must not let such activity draw the Bank away from poverty-focused investment. The IDB is not a regional IMF. The Bank's comparative advantage, like its middle name, is development.

At this point, it may be appropriate for Governors to re-state the terms under which flexibility was granted to accommodate emergency lending. Most important, for us, is the principle that regular development lending, particularly to the poorer countries, must not suffer... and that any deterioration in the Bank's financial ratios must be only temporary. Reserves, net income, and other key indicators must be restored to target levels as quickly as possible—while the Bank redoubles its efforts to meet the agreed GRI-8 targets.

Progress was made on some crucial priorities, such as lending for social projects. Canada is very happy when we see substantial funding used, for example, to bring clean water to the rural poor, or to upgrade and expand their access to education. We are happier still when such efforts take innovative forms which emphasize quality—not just quantity—of programs, involve genuine participation, and include the underprivileged and marginalized. And we are especially pleased when such people—women, children, aboriginals, the disabled—are fully involved as beneficiaries and agents of change. When we see such initiatives, we know the Bank is playing its right role, and our support is well-merited.

We welcome the Bank's commitment to lightening the burden of the heavily indebted poor countries. We also welcome its role in private sector development, in order to create jobs and reduce poverty, through an integrated approach that should start with the Bank's country strategy.

When Governors agreed on the Bank's last capital increase, we endorsed some very important governing principles for the GRI-8 period—principles that remain essential, principles that will help the Bank to weather external shocks and keep faith with its mandate, and with the people of the region.

The Bank should be congratulated for meeting many of those objectives and targets— but some are still to be achieved, such as targets for lending to the poorest countries, and upper bounds set for policy-based lending.

Corporate Governance

The IDB is now at an important stage in renewing its governance structures. Canada has strongly supported the Bank's efforts to improve planning, programming, and efficiency— reflecting the concerns of our taxpayers, who demand transparency and accountability. Such concerns also reflect basic common sense, when resources are limited and value-for-money is vital.

Progress has been made since the 'Managing for Effective Development' exercise—on strengthening Country Offices, on organizing the work of the Board of Directors into functioning committees and working groups, on improving relations between the Board and Management. Much remains to be done—but with solid leadership, there is great potential to improve the Bank's performance, and its impact.

Let me stress once again: we take the targets set by Governors very seriously, seeing them as essential, and not open for renegotiation at every turn. The Board is entrusted with directing the Bank so that these vital objectives are met. Management and Executive Directors should expedite their work accordingly.

By shifting from a culture of control, to a culture of managing for results... by paying more attention to strategic focus... in such ways, we can give the Bank's lending, and the developmental results, greater impact. We welcome the Bank's decision to undertake a corporate strategy and welcome the progress to date. Failure to act decisively will bring increasing risk of irrelevance.

And finally, evaluation... it should be a genuine tool of management, and a catalyst for change. We applaud the IDB's efforts to make the most of borrowing members' capacity for evaluation, through its governance programming in the region. But more still needs to be done to ensure a strong and independent evaluation mechanism in the Bank's own operations.

Conclusion

Our region has a heavy workload for 1999. As Governors meet for the last time in this century, Canada salutes the Bank's hard work and many achievements over the past forty years. And we renew our commitment to helping the Bank play its right regional role—as an innovative, inclusive catalyst of change and progress. Together, we can shape a stronger region, and a brighter future for all its people, in the 21st century.

First of all, I would like to congratulate you, Mr. Chairman, on your election as Chairman of the Fortieth Annual Meeting of the Board of Governors of the Inter-American Development Bank and Fourteenth Annual Meeting of the Board of Governors of the Inter-American Investment Corporation being held in Paris.

I would also like to express heartfelt appreciation to the President of the Bank, Mr. Enrique Iglesias, for his very successful leadership of the Bank and the Corporation.

It is a great honor for me to represent Brazil at this meeting, on such a special occasion, when the Bank is celebrating its fortieth anniversary.

The founding of the Bank was a milestone in inter-American relations, shifting their focus from security issues to the implementation of policies in pursuit of economic cooperation and development in Latin America and the Caribbean.

The idea of establishing a regional financial institution was first raised over a century ago, during the first Conference of American States held in 1889-1890. It later gained momentum in 1947 with the intense economic and social debate sparked with the founding of ECLAC under the umbrella of the United Nations.

The final framework for the design of the Bank was the conference held in Petrópolis, Brazil, at the Hotel Quitandinha, in December 1954. There, for the first time, a cohesive set of proposals on economic cooperation and the establishment of a regional development bank were discussed.

Finally, in 1958, an agreement was reached on the need to launch a regional financial institution. In early 1959 a committee made up of 21 countries was established to negotiate all aspects of the new multilateral lending institution. The ultimate fruit of the committee's work was the Agreement Establishing the Bank, which was signed by the member countries in April 1959.

At this time, I would like to pay homage to two illustrious Latin Americans who played an essential part in the establishment of the Bank. The first of them, thanks to his persistence, tireless work, and technical expertise, after years of hard work towards a great idea, deservedly became the first president of the Bank. I am referring, of course, to Felipe Herrera.

The second, Juscelino Kubitschek, with his statesman's vision, was able to take advantage of the opportunity that arose during a diplomatic crisis in 1958 to demonstrate that Latin American security needed to rest upon prosperity and development. In this way he laid the groundwork for the political understanding that allowed the Bank to be established the following year.

I am pleased to report to this Board that the President of Brazil, Mr. Fernando Henrique Cardoso, has proposed to President Iglesias that an international seminar commemorating the Bank's fortieth anniversary be held this November in the Hotel Quitandinha to discuss the dilemmas faced by Latin America and the Caribbean face in this time of crisis.

Speaking of difficult times, let me turn to the economic crisis that began in Thailand in mid-1997 and later spread to many other Southeast Asian countries.

Its origins can be traced to the dramatic end of a long growth cycle. It stemmed from structural maladjustment in the current accounts of these countries' balance of payments, compounded by fragile financial systems and overvalued assets.

What initially appeared to be a regional problem rapidly became a global crisis. According to a recent study by the World Bank, some 36 countries, representing over 40% of the GDP of developing countries and over a quarter of their population, experienced negative per capita growth in 1998.

The impact of the situation in Southeast Asia reached Brazil in October 1997, when the country successfully thwarted its first speculative attack. The world markets seemed to have returned to normal when, in May 1998, the situation rapidly deteriorated as Russia declared a unilateral moratorium, spreading great unease in the world's financial centers.

We then witnessed a round of capital flight from the emerging economies to unassailably safe assets, mainly United States Treasury bonds.

In the second half of 1998, intense pressure built on the real. Steady losses in international reserves led to a change in the exchange regime in mid-January this year.

The top priority in Brazil's economic policy in the short term is to prevent the scourge of inflation that devastated us for decades from returning, at all costs. At the same time, we must ensure that the stabilization effort does not take place on the backs of the poorest segments of society. I will get back to this point later.

Unfortunately, a recessive scenario has been forecast for the Brazilian economy in 1999. However, the outbreak of inflation driven by the devaluation of the real should be temporary. I am confident that by next year, inflation will have come down to single digits, will be declining, and will be firmly under control. At the same time, the foundations on which sustainable growth can return must have been reestablished.

Structural conditions are quite encouraging for Brazil to be able to overcome the current crisis rapidly. At the political level, we have firmly established democratic institutions and the ability to mobilize the National Congress around the necessary structural reforms. In this connection, I would like to emphasize that the constitutional reforms in the areas of social security and central government administration that are absolutely necessary for the change in the fiscal system were recently approved and are already at the implementation stage.

At the economic level, a series of reforms designed to bring in a more competitive and efficient system of production in Brazil have been carried out in the past few years. The most noteworthy are as follows:

- (a) The process of economic liberalization has been deepened with air across-the-board reduction in tariffs and the elimination of administrative barriers to imports.
- (b) A number of monopolies have been broken up, in the areas of oil and natural gas, shipping, and telecommunications.
- (c) The privatization program has been accelerated, and has now covered iron and steel, mining, rail transportation, ports, telecommunications, and power distribution, and the process of privatizing power generation has been launched.
- (d) Investments in infrastructure have been increased, with strong private-sector participation.

The privatization process also encompassed the financial system, with the sale of several major State-owned banks. It should be recalled that, under the *Real Plan*, a broad program was undertaken to restructure the banking system, including private banks. The system has therefore been relatively resistant to the impact of the economic downturn and higher interest rates.

Regarding macroeconomic policies, the greatest change under way is that the gradual approach to adjusting government accounts has been replaced with an immediate, far-reaching change in the fiscal system, consolidating its restructuring at the three levels of government: federal, state, and municipal.

Under the understanding reached with the IMF last week, we agreed to generate a primary surplus of 3.1% of GDP in 1999, 3.25% in the year 2000, and 3.35% in 2001. This strengthened fiscal adjustment and the institution of the free exchange rate regime should allow the real interest rate to decline significantly. The objective of reducing the public debt-to-GDP ratio will thus become feasible, even in 1999, as well as a substantial decrease in the following years.

Special care was taken in the budget cuts to ensure that the decrease in spending would not affect basic social programs in education, vocational training, health, unemployment insurance, and social welfare. This was also the basis for one of the emergency loans approved by the Board of Executive Directors of the Bank last week.

I would like to take this opportunity to express the appreciation of President Fernando Henrique Cardoso to all those who contributed to the successful outcome of this complex financial operation, especially to President Iglesias, Executive Vice President Burke Dillon, and to the member countries, which supported its approval through their Executive Directors.

To return again to the IDB's history of success, this is a good occasion to reflect on the course we should take in the future. In an initial phase, the Bank's activities consisted of providing substantial amounts of capital for infrastructure development in Latin America. More recently, the scope of its activities has expanded significantly. Higher priority has been given to the social areas, and in particular projects designed to reduce poverty and inequality.

The IDB has lent invaluable support during emergency situations caused by natural phenomena as well as economic and financial problems. It has also promoted projects and programs intended to intensify regional cooperation at all levels.

Despite the undeniable progress achieved over the past 40 years, the countries of Latin America and the Caribbean must still find solutions to many problems.

Poverty and inequality remain at intolerably high levels in most countries of the region. Our economies continue to be extremely vulnerable, as shown by the acute impact of the international financial crisis on our countries.

On the positive side, we must maintain the progress we have made in fighting chronic inflation, one of the greatest stumbling blocks to growth.

Additional and continued effort is needed to improve the external competitive position of our economies. Like it or not, there is every sign that globalization is here to stay. We must learn to profit from it.

Still a high priority on our agenda is progress toward regional integration, an area in which the global financial crisis has produced considerable tension.

Today, we can see clearly that development is a complex process that hinges upon the accumulation of capital and investment in education, professional skills, and research and development.

A broader conception of the development process also encompasses our political, juridical and economic institutions, particularly in relation to minimum standards of income distribution and social justice as keys to stability, a prerequisite for forward-looking long-term planning.

Ultimately, the main objectives of development are to reconcile efficiency with equity on the economic front, and freedom with justice on the political front.

Clearly, President Kubitschek's vision that the security of Latin America and the Caribbean depended not on repression but on development and social justice remains more valid today than ever. However, the world has become much more complex, and the challenges facing the IDB in the new millennium are formidable.

Finally, allow me to express my sincere thanks to the people and Government of France, and this marvelous city of Paris in particular, for the warm welcome they have extended to us in hosting this event.

ADDRESSES

THIRD PLENARY SESSION

MARCH 16, 1999

As the world has seen, 1998 was a difficult year for the region, and therefore for the Bank as well. The year was marked by both climatic and financial emergencies. Having contributed for many years to macroeconomic adjustment in the countries of the region, the Bank now had to devote considerable resources and time to these emergencies, to the detriment of its traditional lending program.

Nevertheless, the need to respond to the difficulties in the region in 1998 allowed the Bank to reassert its social mission and also to resolve other recurring problems not directly related to the difficulties. The activities it carried out in Central America after Hurricane Mitch, for instance, enabled it to make up for delays in implementing the HIPC initiative. The Bank has also distinguished itself as the main advocate of special treatment for Honduras and Nicaragua.

From a humanitarian perspective, the balance-of-payments support provided by the Bank in 1998 was less urgent, but enabled it to take part in a global effort to protect middle-income countries in the region against contagion from the Asian crisis. However, the cost of this support has been high, deviating a substantial amount of the Bank's resources from its primary purpose and increasing the financial exposure. Despite a high opportunity cost—30% of lending in 1998 and perhaps more in 1999—this assistance has also contributed towards resolving the problem of depletion of the FSO concessional resources.

Several member countries, including Belgium, would have preferred an approach taken in other multilateral institutions—allocating a portion of the income from the special emergency loans to finance certain initiatives, such as technical assistance and the HIPC initiative, threatened by the FSO's inability to generate income and reserves.

However, Belgium considers last year's performance positive on the whole, provided that the following two conditions are met.

First of all, financial emergency loans must remain exceptional. The primary focus of the Bank should continue to be support for structural reforms and poverty reduction in the region. This approach should be reflected in—among other measures—reinstatement of the well-known 15% and 65% caps, on the understanding that the IMF should continue to play the role of lender of last resort. It is up to the Fund's membership to ensure that it has enough resources to do so. Recent developments in Brazil's financial situation demonstrate the ad hoc nature of the emergency measures taken. Accordingly, the IDB needs guidelines that should be established as soon as possible so that they can be followed at the first signs of a balance-of-payments crisis.

Secondly, in the spirit of the Eighth General Increase in Resources, the Bank should reassign priority as soon as possible to the fight against poverty, which, in the eyes of the governments and the general public, has become the primary reason for the industrialized countries joining the Bank and for the efforts made during the last capital replenishments. Actually, the goals of macroeconomic stabilization and greater equality are linked. The Bank itself in its report entitled *Facing Up to Inequality in Latin America* indicated that too much inequality is an obstacle to economic growth. It is also helpful to recall that too much inequality leads to more violence and crime, which can become obstacles to investments. Moreover, poor allocation of budget resources translates into high, destabilizing deficits. Such unsustainable budget deficits, symptomatic of improper governance, are precisely what led to the financial crisis due to contagion. In fact, it is possible that the budget policies in force prior to the crisis would sooner or later have led to a balance-of-payments crisis and that the contagion effect of the Asian crisis only precipitated it.

Under the Eighth Replenishment, the Bank set a special goal: to gradually increase the proportion of lending for the social sectors to 40% of the total lending. Unfortunately, the statistics for 1995 to 1998 show that less than 30% of approvals were for the social sectors in the broad sense, that is education, health, water supply, sanitation, and microenterprise. Moreover, the figure for 1998 is already an overestimate since emergency loans for natural disaster relief have been included. The Bank must therefore return to its goals as soon as possible.

Given that each operation is submitted to us as being more or less directly or indirectly poverty-targeted, we would refocus social sector loans on the basic subsectors—health and education—that bring the greatest direct benefits to the neediest segments of the population and promote coordination among donors and specialized agencies in other social sectors.

It is also essential that the standard of good governance be more systematically incorporated into lending policies. Good governance has been shown to be a prerequisite for development aid to be able to contribute effectively towards poverty reduction.

Another major challenge will be to promote crossover issues such as the role of women in development, the environment, and indigenous populations, so that these issues become a concern for all the member countries. Their basic contribution to better development will largely offset the high short-term costs they entail.

Furthermore, the Bank should ensure that it allocates its resources to activities directly connected with the projects and programs. In our opinion, certain so-called nonfinancial activities have at this point grown so much that others are at risk of being crowded out.

With regard to financial matters, I would like to commend the Bank and the Finance Department for their active, intelligent management of the Bank's resources. I am referring in particular to the introduction of new instruments that better protect, and even increase, the Bank's net income.

Lastly, I would like to express my heartfelt thanks to the authorities and people of France and of Paris for hosting the meeting and for their hospitality. I have also been asked by the Governor for Belgium, Minister Jean-Jacques Viseur, to convey his best wishes for a fully successful meeting.

I am pleased to have this opportunity to address the Annual Meeting in this radiant City of Lights. I would like to commend the authorities for the superb organization of this event—the last one in this millennium—which is taking place on the eve of a new century, in a renewed Europe that is prepared to take on the challenges of integration, open to the developing world.

This has been a difficult year for the region. The sharp deterioration in the terms of trade, market volatility, reform programs still to be implemented, and the distressing presence of inequity and poverty bring home the fact that market forces alone cannot resolve all the problems and that the State must remain a presence. The multilateral banks have an important role to play here—as important today as when these institutions made their mid-century appearance in the development world.

In this setting and on the threshold of the new millennium, democracy in Venezuela, under President Chávez's administration, is entailing a deep-seated renewal, a rethinking of the State, and efforts to instill the necessary governance to efficiently and effectively address the numerous problems besetting our society. Hence the importance of the forthcoming constitutional reshaping process, which is gradually surmounting various obstacles and should come to fruition this year.

In 1998, owing to the precipitous drop in oil prices, Venezuela had to rewrite its budget throughout the year in order to bring spending into line with much-reduced oil and nonoil revenues. For the first time, general tax revenues far exceeded revenues from oil sales.

The result was a fiscal deficit equivalent to 4.8 percent of gross domestic product, which was addressed by way of cutbacks in government spending, with preference given to the use of internal resources, limited use of voluntary markets, and resources from multilateral banks, notably the Inter-American Development Bank.

The difficulties that arose in 1998 seem to be worsening in 1999. The new administration is faced with a substantial fiscal deficit approaching 8 percent of GDP and oil prices are still low, adversely affecting the balance-of-payments current account and ordinary Treasury revenues. The situation has been further undermined by inflation. Although rates did edge down in 1998, inflation is still high, eroding the purchasing power of real wages and causing living standards and the quality of life in Venezuela to decline.

As one of its first measures, the government adopted a stringent fiscal adjustment program to deal with our heavily imbalanced accounts. The 1999 budget has been revised with revenues recalculated on the basis of a lower export price for oil. As a result, oil revenues will defray less than 35 percent of total spending for the year. The new state of affairs therefore demands a rethinking of the country's development strategy.

The Venezuelan government seeks to achieve sustained growth in the production apparatus over the medium term in a participatory, democratic setting in which it will be possible to reverse the inequitable distribution of income and alleviate poverty. The cornerstone of economic policy must therefore be to curb inflation. This will be attained by instituting a cohesive economic program aimed at stabilizing the major aggregates, creating employment, and freeing up the factors of production, which have been constrained by various elements that have caused the country's production apparatus to stagnate.

First, however, we will need to overcome the problems that exist in this year of transition. Tackling the deficit is the main economic imperative now. In addition to the budgetary retrenchment noted earlier, the Parliament is also considering granting the President of the Republic the power to issue, as extraordinary measures, a series of decrees whereby ordinary revenues could be raised by just over one percent of GDP; by levying a temporary tax on bank withdrawals, gradually converting the luxury tax and wholesale tax into a general sales tax, revising the present income tax, and revamping the tax and customs administration. The legislation also provides for an integrated public finance management system, which would substantially improve domestic fiscal-policy management.

In addition, the use of this instrument will mean removing obstacles with respect to the regimen of the central and decentralized federal government, facilitating private-sector involvement in economic activity, and strengthening financing mechanisms for such activities.

Accordingly, the economic program includes, in addition to the aforementioned fiscal adjustments, new taxes and administrative reforms to boost revenues and rationalize spending. However, even with the government's efforts to trim operating expenses, the external debt service burden is still considerable. In the early months of the year, a strategy was adopted to raise funds in the domestic market in order to cover the cash-flow requirements for internal and external obligations. Various options are also being explored to penetrate the external voluntary markets.

Although spending has been pared considerably, every possible effort has been made to maintain spending to protect human capital, such as the education and health agency budgets, expenditures for children's services, and all programs that seek to improve the situation of low-income groups.

Initial actions have been taken to reverse the decline in the quality of life of the very poor, and a set of emergency actions devised will enable the government, in its first 18 months, to generate employment and income for Venezuelan families.

As to monetary and exchange-rate policy, the close coordination established in 1998 between decision-making bodies remains in place. As a result of this coordination, interest rates have been falling bit by bit. The bolívar is in the lower range of its band and

international reserves stand at one year of imports, in spite of the decline in our country's leading source of foreign-exchange earnings: petroleum and petroleum products. Of concern, however, is the deep economic recession. Steps have been taken to promote selected sectors including gas, petrochemicals, tourism, agriculture, and industry, particularly small and medium-sized industry.

As part of efforts to promote and afford legal certainty for foreign investment, a new Investment Act and an amended Concessions Act are on the official agenda, so we may say, with some optimism, that signs of recovery could be noted in the last quarter of the year.

The region is passing through a difficult period. Turmoil in financial markets and natural disasters have added further pressure to the already exacting task of development. But our countries have stayed the course, endeavoring to build their economies within the framework of macroeconomic programs that favor fundamental balances, while striving for viable structural change and creating conditions for sustainable development.

In this context of fiscal austerity, the solidary effort by countries in the region to provide concessional resources to the Bank through the conversion of local currencies marks a milestone for the institution. By way of this agreement, even the less developed borrowing member countries are contributing resources to the solution. Yet, the shareholders with the greatest economic potential are notably absent in the search for avenues of solution. We are confident that decisive action by the borrowing countries and the leadership of the President of the Bank will encourage this group of countries, our friends, to take steps to increase concessional resources by accelerating convertible-currency FSO payments and by way of fresh contributions, including those that could support financing of resources for the Heavily Indebted Poor Countries initiative.

Venezuela's position is backed by our longstanding stance of participating actively and generously in efforts since the 1970s to help make more IDB concessional resources available. We should remember that, since that era, our country has made its local currency available to the borrowing member countries. It was the Board of Governors' decision that Venezuela, like Mexico, would not have access to optional loans.

Concessional resources make programs and projects in countries unable to meet the ordinary-capital terms and conditions financially viable, while preserving the institution's sound financial position. We must bear in mind, however, that those resources make it possible to finance other activities and satisfy a series of needs that would otherwise remain unmet. It is essential therefore to ensure, as from this year, that concessional resources in local currency will be available for all borrowing countries.

We would like to acknowledge the work done this last year by the working groups of the Board of Executive Directors and the Management of the Bank to review and reshape various procedures, programs, and projects that have a direct impact on the functioning of the institution.

Meanwhile, we must continue working on the Bank's medium-range vision and determine how it fits into the new international financial architecture, and what role falls to it with respect to the needs in the region. One tangible result has been the development of an emergency lending facility to help countries contend with the present crisis.

Inasmuch as this new product has put pressure on some of the Bank's financial indicators and fast-disbursing loan capacity, we believe that a set of criteria would need to be established to facilitate the country distribution of resources of this kind.

The Inter-American Investment Corporation's capital increase will improve the institution's financial situation. The admission of new members, which we welcome, will bring ideas and capital from these countries to our private-sector investments. In this new cycle, we must continue to pursue our broad lines of action, supporting the efforts of the region's entrepreneurs in the global marketplace, giving the private sector a role in resolving the infrastructure deficit, and continuing to foster efforts whereby the initiative and energy of our peoples can translate into true enterprises.

The challenge for the Multilateral Investment Fund will be continued innovation, to constantly explore original approaches to support the private sector and our microentrepreneurs.

In closing, Mr. President, we salute you for your stewardship of the Inter-American Development Bank. Thanks to your efforts, our institution is becoming stronger by the day, and is answering the needs of the region. We welcome our new Executive Vice President, Ms. Burke Dillon, to the Bank's team. We are confident that she will soon assimilate the culture of our institution, whose excellent staff has a wealth of experience in the task of development project support, design, implementation, and evaluation.

To conclude, I would like to reiterate our appreciation for the Bank's continued presence as the region rises to the many challenges that await it in the new millennium. In this next chapter, the technical and financial assistance provided by our Bank, and our President's demonstrated leadership, will be needed more than ever.

The Dominican delegation is very pleased that this Fortieth Annual Meeting of the Board of Governors of the Inter-American Development Bank and Fourteenth Annual Meeting of the Inter-American Investment Corporation is being held in Paris, the cultural capital of the world, the heritage of mankind, and the cradle of the ideals of liberty, equality, and fraternity. We are also delighted with the meeting's excellent organization and with the wonderful hospitality of our hosts from this unique city. In addition, we would like to pass on a special greeting from the President of the Dominican Republic, Dr. Leonel Fernández, who expects that these meetings will be as beneficial for the region as they have been in the past.

We would like to point out that this year we are celebrating the fortieth anniversary of the Inter-American Development Bank. We believe that the aspirations of the visionaries who founded the Bank have been fulfilled over the course of these four decades, during which time this institution has played a leading role in the economic and social development of the region under the skillful guidance of Presidents Felipe Herrera, Antonio Ortiz Mena, and Enrique Iglesias.

The Bank's forty years of activity have been critical in supporting material, economic, and social progress in the region. The IDB has provided more than US\$95 billion in loans, which has made it possible to generate US\$240 billion in investment toward the priorities of the borrowing countries. Just last year, the Bank approved loans worth a record total of US\$10 billion, and it did this at a critical time, allowing the region to confront financial pressures on their economies.

We would like to reiterate our support for all actions directed at facilitating the process of delegating authority in order to strengthen the Country Offices. Also of note is the hiring of consultants with funds from the Action Plan for Group C and D countries in order to accelerate the implementation of some projects. With regard to the Dominican Republic, a significant role was played by President Enrique Iglesias, the Bank's Management, and the Bank's Country Offices in designing the emergency loan and reformulating projects under way, in the aftermath of Hurricane Georges. We would like to use this opportunity to propose the loosening of requirements for the disbursement of sector loans to countries that have been adversely affected by unusual weather conditions and are eligible for emergency financing.

We welcome the agreements that have been reached with regard to concessional resources. During the last several meetings, we have maintained that the use of these resources by less-developed countries in the region would allow them to undertake development projects on favorable financial terms. For this reason, we accorded priority to these issues during the previous meetings. The commitment and efforts of the countries of the region should be emphasized, since we will be assuming the costs of the agreements. The solution that was reached with regard to concessional resources will have a significant effect on the economic development of the countries that made a commitment to contribute local currency. In the case of the Dominican Republic, the conversion of local currency will have an impact on applying prudent monetary policy.

We strongly endorse efforts to increase the capital of the Inter-American Investment Corporation (IIC), since this will provide major support for small and medium-sized enterprises in the region. We view this increase favorably and welcome the entry of new members into the Corporation.

In 1998, Latin America was affected by natural disasters that had a serious impact on the economic structures of several countries in the region. The "El Niño" event, the severe droughts and floods it brought in its train, and the devastating effects of hurricane Georges and Hurricane Mitch in the Caribbean, Mexico and Central America claimed many human victims and caused considerable damage to infrastructure and production facilities. These disasters have increased the financial demands of rebuilding the affected areas, and the multilateral organizations, especially the Inter-American Development Bank, have responded quickly.

In addition, the region was forced to deal with the effects of the crises in Asia and Russia, which led to a drop in commodity prices, especially oil and mineral ores, and to short-term capital flight. As a result, economic growth in Latin America has slowed. Nevertheless, the region had an above-average rate of growth in 1998, and inflation stabilized at 10 percent.

We therefore understand the reasons that have led the Bank to promote emergency financial loans, which represent special effort in support of the countries of the region to mitigate the negative effects of the global financial crisis. The significant amount of resources earmarked for these loans could eventually affect the future availability of funds for regular programs that are vital for the small and medium-sized economies of the region. We trust that this initiative will not affect policy-based loans in various sectors.

I would now like to touch on the economic performance of the Dominican Republic during the last year. The Dominican economy continued to post strong growth in 1998, expanding by 7.3 percent in real terms, the highest level in the region according to statistics provided by ECLAC. This places the country's average growth rate over the last three years at 7.6 percent. Meanwhile, single-digit inflation (7.8 percent) was maintained for the fourth year in a row. All of the above occurred in spite of the damage caused by Hurricane Georges, which according to natural disaster experts and ECLAC amounted to US\$2.144 billion, of which US\$1.521 billion represented losses in assets.

Furthermore, per capita GDP increased by 4.9 percent, more than twice the 2.3 percent rate of population growth, thus leading to an increase in real income. This growth was also reflected in an improved employment situation, with unemployment falling from 15.9 percent in 1997 to 14.3 percent in 1998 and the creation of more than 200,000 new jobs.

In spite of the above-mentioned natural disaster, the country's net international reserves rose to US\$100 million in 1998. There was a surplus in the overall balance of payments, although the current account had a deficit of 2.4 percent of GDP owing to higher

imports as a result the hurricane. Meanwhile, the capital account recorded a surplus, mainly due to an increased flow of direct foreign investment to tourism, duty-free zones, and telecommunications.

On the fiscal front, the government had a balanced budget through the appropriate management of expenditures and more efficient tax collection while following a policy that favored the social sectors—particularly health, education, and environmental protection—as well as the reconstruction of hurricane-effected infrastructure. In this respect, we have had the technical and financial support of the IDB and the World Bank.

The public sector, however, continued to be a net exporter of capital. For each dollar that the Dominican Republic received in 1998, it paid its creditors the equivalent of \$US1.80, despite receiving resources from the IMF, through the repurchase of 25 percent of our quota, and a 6-month deferment from the Club of Paris on debt payments falling due between September 1998 and March 1999. Venezuela, for its part, demonstrated continued support for, and solidarity with, the Dominican Republic by refinancing the debt for the above-referenced period over a term of five years.

In this same vein, although the 6-month deferment from the Club of Paris on foreign debt payments represented important temporary relief in support of the national reconstruction program, it is also true that a nation affected by a hurricane of this magnitude cannot be rebuilt in a period of six months. In this regard, I would like to mention that, in our case, the international payment commitments derived from the above-referenced Club of Paris deferment will represent additional expenditures of 1.5 percent of GDP in 1999, a figure which does not include the needed financial resources for continuing the task of reconstruction. As you can see, this means that the country will have to make an extraordinary effort to maintain the macroeconomic stability that it has enjoyed over the last few years.

This year, it is estimated that the Dominican economy will grow at a rate of 7 percent with 6 percent inflation, according to the Central Bank's monetary program. Achieving these objectives is predicated on the adoption of a balanced-budget fiscal policy.

The Dominican Republic is currently pursuing an active foreign policy under the personal direction of President Fernández that has resulted in the signing of a free trade agreement with Central America and advanced negotiations with CARICOM. Last year, investment-protection agreements were signed with France, Chile, Ecuador, and Taiwan. Meanwhile, missions headed by the President himself resulted in attracting new investment for modern infrastructure in the areas of energy, urban development, environment, and tourism, while progress was made in the effort to reform and privatize public enterprises. To this end, international bidding processes have already been initiated in order to attract foreign investment to these business areas.

Next month, the Second Summit of Heads of State and of Government of the Association of Caribbean States will be held in Santo Domingo for the purpose of increasing trade and cooperation. In November of this year, more than 50 leaders of ACP States will meet in our country for discussions regarding a successor to the Lomé IV Agreement.

If we look back over the last forty years, Latin America and the Caribbean have made great strides toward strengthening democracy, economic development, and social justice. In this regard, we have been able to count on the significant and timely support of the IDB. This considerable progress underscores the importance and the necessity of strengthening ties of solidarity and cooperation throughout the hemisphere as a way of addressing the challenges of the Twenty-first Century. These meetings, therefore, are step in the right direction.

We wish to express our sincere gratitude to our hosts, the French government, for the warm welcome they have given us. It is a great pleasure to share with you, here in this beautiful city, our experiences in implementing the program of economic and social reforms carried out by our government since the end of 1994, and our accomplishments so far.

First, we would like to welcome the new Executive Vice President, Mrs. BurkeDillon, and wish her every success in her tenure with the Bank.

Since our government came to power, we have shared with you at these annual meetings the progress that has been achieved in respect to economic and social reforms in Panama. We would now like to provide a brief overview of the situation as of the beginning of our administration, as well as of the work carried out and the most significant events of the last twelve months.

In 1994, the Panamanian economy was made up of two distinct sectors, each with its own well-defined characteristics: one, a modern and expanding sector integrated with international trade, and the other linked to domestic activity, having reached the end of its growth cycle. For decades, the second had been subject to protectionist policies which had pushed domestic prices higher than world levels, obstructing relations with external markets, raising consumer prices, and reducing competitiveness in export-related activities.

This administration was faced with the challenge of introducing economic reforms over a short time period which would strengthen the sources of growth, open up the economy, and at the same time maintain a proper fiscal balance. This set of reforms was, from the beginning, aimed at revitalizing economic growth, creating jobs and modernizing the country in readiness for the new millennium and the country's assumption of the Panama Canal administration beginning January 1, 2000.

Our program included reform of the economy's legal framework to boost competition in the various sectors. To this end, the labor code was reformed, a modern law encouraging competition was passed, progress in trade reform was achieved and a program of restructuring, privatization and concessions in major public services was implemented.

At the same time, trade reform substantially reduced excessive protectionism, placing the tariff ceiling at 15 percent, with only a small number of exceptions.

Under the privatization program, the ports of Balboa and Cristobal, located at the entrances to the Canal, were turned over to concession, and concessions were also granted for constructing two new, modern container ports on the Atlantic coast and for the trans-isthmus railroad which, once modernized, will connect all the ports.

In 1997, the telephone service was successfully privatized and concessions were granted for two cellular service bands. In 1998, after dividing the electric power enterprise into eight separate companies, a 51 percent interest in the three distribution companies resulting from that division, along with the thermoelectric enterprise, was privatized, as well as a 49 percent share of the companies generating hydroelectric power. The transmission enterprise remained a wholly-owned government corporation. The privatization process in the electric power sector was successfully completed at the end of 1998.

Our government has devoted particular attention to the management of public finance. The trade reform program, and the privatization and concessions were designed to minimize any adverse impact on public finance. At the same time, a deficit ridden supplementary retirement plan for public officials was converted to a self-financing system of individual pension accounts; this program, now in its final stages, is due to begin operating in the middle of this year.

In terms of external debt, our government was successful in reaching an agreement on rescheduling payments, while obtaining a reduction in the overall amount. This came about after a process involving the use of Brady bonds and a successful bond issues and debt repurchase program, following a long absence from the international financial markets.

Now, four and a half years after reforms began, the overall record of this administration can be considered to be positive. Trade reform has brought competition to the domestic market, which has begun the process of bringing down prices for goods. At the same time, modernization of industry and of technology in the previously-protected sectors—segments of the economy that were lacking in competitiveness—is under way. For the first time the country as a whole is looking to world markets as the way to promote economic growth.

The privatizations and the concessions granted have served to develop and modernize the ports to such a degree that in the not so distant future the country has real prospects with the air, land and rail links, of becoming a regional center for freight handling and distribution. It is worth mentioning that the annual rate of growth in port-related activity has exceeded 20 percent in the last two years.

Another important aspect of the privatizations is the transfer of responsibility for investment from the public to the private sector. It is estimated that in the next five to ten years the private sector will invest approximately B3 billion in the process of modernizing and expanding services which, until recently, were under government control, significantly increasing private sector participation in the economy and ensuring that investment will occur which otherwise would have had to be absorbed in the public sector investment program.

Another important achievement of our reform program was reversing the downward trend in the economy's growth rate. As of 1996, the economy has posted positive GDP growth and, in 1998, despite the adverse effects of climate factors and the international financial crisis, the growth rate was 3.9 percent, with the rate for 1999 estimated to reach 4 percent.

We are particularly pleased to highlight the bond ratings assigned to Panama by the international rating services. This reflects the orderly management of our public finances and the positive effects of the reform program on economic performance. Today, Panama has one of the highest ratings among emerging countries.

Despite the international financial crisis, Panama continues to attract the attention of investors, due to the absence of exchange risk, low levels of inflation, and the stability demonstrated in recent years.

The current administration feels satisfied with the work carried out and the progress achieved. We are confident that consolidating our economic reforms will be vital to the future development of our country. Moreover, we are convinced that regardless of who prevails in the next elections, our program to modernize and open up the economy will proceed at the necessary pace.

Mr. President, last year the IDB approved a record number of operations for the Republic of Panama. Notable among these is the Darién sustainable development program to which we, like you, are particularly committed.

Finally, we wish to express, once again, our profound gratitude to the President of the Bank for his personal support and participation in the management and approval of the lending program implemented over the last few years. We would like to reiterate our commitment to the development of our country, in particular, of less advantaged groups.

First of all, I would like to thank the Government of France for organizing this meeting, as well as the city and people of Paris for their hospitality and cooperation. I would also like to congratulate the Bank's new Executive Vice President, Ms. Dillon. We hope she will be very successful, and we offer her our full cooperation.

At last year's meeting, we indicated that 1997 had been a year of economic expansion. Now, after a 1998 that was full of uncertainty and surprises, we begin 1999 with a combination of concern and hope.

For Latin America and the world, 1998 was a year of numerous unforeseen events that have had a considerable impact on the Bank's activities. During 1998, there was a considerable increase in the instability of financial markets, and Latin America and the Caribbean were severely affected by several natural phenomena.

In the second half of the year, the instability of financial markets finally had an effect on the rate of growth in Latin America, which declined from 5.3 percent in 1997 to 2.5 percent in 1998.

Although we cannot say that the uncertainty has disappeared completely, this unstable situation has brought two positive factors to the fore: first, an across-the-board, rapid response by Latin American governments, which implemented consistent macroeconomic policies and structural reforms and, second, the equally rapid support of the international financial system as a whole and of the Inter-American Development Bank in particular.

Perhaps the most important example of this concerted international response was the establishment of the multilateral financial-support package for Brazil, to which Spain contributed \$1 billion.

During the past year, the Bank has also had to deal with the natural disasters that devastated various countries in the region. The floods caused by the climate changes associated with the "El Niño" phenomenon, hurricanes "Georges" and "Mitch," and, most recently, the earthquake in Colombia, have elicited a prompt and decisive response by the Bank.

As a matter of course and in accordance with our bilateral policy, we support the Bank's actions to assist all of the countries that were affected by the natural disasters, and we are also pleased with the success of the Consultative Group on Central America. To ensure that the assistance is effective, we believe that the Bank should play a leadership role in coordinating it.

This is the context in which we must judge the Bank's activities. As a result, 1998 may be described as a year of transition, not only because of the events described earlier, but also because of several reforms that have either been implemented or are in the process of being implemented.

During this period, three changes have been made that may be of particular importance for IDB activities over the next few years: first, the provision of sufficient resources to fulfill the long-term need for concessional facilities; second, the introduction of an emergency lending facility; and, third, changes in the support mechanisms for the private sector.

The provision of sufficient concessional resources to attend to the needs of the poorest countries of the region through the year 2009, including the participation of Nicaragua and possibly Honduras in the HIPC initiative, demonstrates that the Bank, in a climate of institutional maturity, is characterized by a spirit of cooperation and solidarity among its members. This achievement is attributable to the acceptance of general conversion of local-currency holdings, previously not convertible, deposited in the member countries.

The approval of a new emergency lending facility allowed the Bank to participate in international financial assistance aimed at lessening the impact of financial instability on the region. However, this new area of activity should be compatible with fulfilling the objectives of the Eighth Replenishment.

In 1998, we also approved changing the operational limit on the activities of the Private Sector Department. The new ceiling, which will make it possible to satisfy existing demand more fully, is only part of the movement toward the private sector; the decision to increase the Corporation's capital and consolidate the Multilateral Investment Fund reaffirms the Group's commitment in this direction. This tendency should lead us to redouble our efforts to increase the efficiency of all aspects of our support for the private sector, increasing coordination between programs and with other institutions having similar goals.

Within the context of transition, I would also like to make reference to the Bank's mission under its current mandate. We are pleased with the consolidation of activities in areas that have been promoted recently: State reform, the status of women, support for civil society, and support for the harmonious, integrated development of indigenous populations and communities.

With regard to the Bank's future, it is critical that the complexity associated with having numerous objectives—a characteristic of development assistance—be reconciled with the flexibility and organization that are necessary for efficient action. Reforms should serve to improve program preparation, to streamline administrative procedures, and to increase internal transparency. In addition, closer collaboration should be sought with other institutions in contributing to the effort to increase the stability of the international financial system.

It should not be forgotten that the various international monetary and financial institutions were created for the purpose of implementing international economic policies that reflect the foreign economic policies of member countries. This objective is even more important in an increasingly interrelated world in which capital movements are playing an increasingly significant role.

In today's world, coordinating foreign and domestic economic policy is essential in order to ensure a stable economic environment. The recent monetary integration of Europe only confirms this realization.

I mentioned earlier that we begin 1999 with a combination of concern and hope. As I have already indicated, the appropriate response by all those involved in 1998 gives us reason for optimism even in the current situation. But the basic reason for facing the future with hope is the wisdom with which the Bank has established its new areas of activity. Its advisory activities with respect to institutional reform and sector liberalization, especially in connection with financial sector reform and support for private enterprise, provide a guarantee of sustainable growth over the long term.

Continuing our efforts to consolidate these areas of activity will contribute to diminishing uncertainty and will allow the Bank to continue to efficiently fulfill all aspects of its mission in support of the economic and social development of Latin America and the Caribbean.

I can assure you that, as always, the Bank can count on our full support in pursuit of this mission.

It is a great pleasure for me to attend this Fortieth Annual Meeting of the Board of Governors of the Inter-American Development Bank and Fourteenth Meeting of the Inter-American Investment Corporation. On behalf of the Mexican delegation, I want to thank the Government of France and the people and authorities of Paris for the hospitality they have extended to all participants.

I also want to extend my warmest welcome to Ms. K. Burke Dillon as Executive Vice President of the Bank. I know that the Bank will be enriched by Ms. Dillon's expertise and experience, and I wish her every success. I would also like to express our gratitude for the tireless and capable efforts of Ms. Nancy Birdsall.

As everyone is aware, 1998 was an especially tough year for the international economy and in particular for the so-called emerging economies. The collapse of international prices for major commodities was compounded by the flight of capital seeking lower-risk assets in other countries, and such economies were virtually shut out from further borrowing in capital markets.

The magnitude and intensity of this phenomenon, which were unprecedented in many respects, were difficult to foresee. This was evident in the repeated downward revisions that have had to be made in predictions for global economic growth.

Mexico fell victim in particular to the collapse of world oil prices, which resulted in fiscal revenue losses equal to 1.3 percent of our GDP. At the same time, the volatility of international financial markets created pressures on the exchange rate and tended to boost interest rates and inflation.

Faced with such a situation, the only realistic path was to cut back on public spending. By doing so, we were able to mitigate the adverse effects of these shocks and absorb them in an orderly way, and thus protect economic growth and continue to create jobs.

This meant that public spending went through three successive trimmings in the course of the year. As well, we adopted a tighter monetary policy in order to help reduce market volatility.

The success of these measures was due to the fact that Mexico's economic fundamentals were already sound, thanks to its policy of fiscal and monetary discipline, its prudent management of the public debt, its flexible exchange rate, its stronger domestic savings performance, and the diversification of the products it sells on the world market.

These factors taken together meant that the Mexican economy has had satisfactory results to show for the past year.

The economy grew by 4.8 percent in real terms, a rate that was the highest in Latin America and one of the highest in the world.

Job creation surged ahead. During this last December we enjoyed our lowest open unemployment rate for the month in six years, and in January the rate was the lowest for that month in eight years.

Inflation during 1998 stood at 18.6 percent, 6.6 points above expectations. This was due to a greater-than-expected depreciation of the nominal exchange rate, under the impact of international volatility. Yet inflation for the first two months of 1999 has shown a clear downward trend, and suggests that we will be able to meet our goal of around 13 percent for the year as a whole.

Despite the enhanced competitiveness of Asian products, in light of that area's significant currency devaluations, and despite slower growth in the world economy and plummeting international oil prices, our total exports managed an increase of 6.4 percent, and in fact our non-oil exports grew by 11.3 percent.

These positive economic results were a key factor in the successful placement of a one-billion dollar bond issue on February 5 this year, which was also a sign of confidence in our country's economic outlook. This was the first bond issue this year by a Latin American country on the dollar market. It was followed by a Pemex bond issue of a billion dollars, and another by NAFINSA for 300 million dollars. And now, during the IDB meeting here in Paris, we have concluded an operation whereby we are refinancing in advance the bulk of the stand-by liquidity line that we arranged last October, and that was due to expire in April of next year. This agreement allows us to refinance some 1.9 billion dollars on medium and long terms, out of a total of just under 2.7 billion. It will help to instill confidence in the Mexican economy as we head toward a change of government in the year 2000.

Mexico has succeeded in a relatively short time in absorbing the instability unleashed by the devaluation of the Brazilian *real* at the start of the year. In the past eight weeks, interest rates have fallen by more than 10 percentage points, the exchange rate has appreciated by more than 10 percent, and the Mexican stock exchange index has gained 45 percent in nominal terms.

Having succeeded in consolidating economic growth and boosting employment in 1998, the federal government has now put forward a responsible and prudent economic program intended to keep economic growth as high as possible and prepare the way for a smooth transition to a new administration. The Congress has thus been asked for the first time to consider a two-year economic program that sets goals for both 1999 and the year 2000.

In spite of the discouraging international setting and the likely persistence of low oil prices, we expect that our GDP will record an increase of 3 percent this year and 5 percent for the year 2000.

With respect to the fiscal deficit, Mexico's target for the current year is to keep it to 1.25 percent of GDP, and 1 percent in 2000. Achieving these goals will mean subjecting program expenditure to heavy restrictions, although we shall continue to give special consideration to social spending, in particular the war on poverty, and to strengthening federalism. In 1999, social spending will account for 60 percent of programmable expenditure.

Another key element in maintaining a dynamic economy is the implementation of structural reforms. In recent years we have in fact recorded some major achievements, with respect to ports, airports, railways, telecommunications, reforming the social security system and the financial sector, among others. More recently, President Zedillo submitted to Congress a far-reaching initiative to open the electric power sector to domestic and foreign private investment.

We are pleased to note that 1998 was an especially fruitful year for the IDB. Together with the leadership shown by Enrique Iglesias and the Bank in helping our sister countries of Central America to recover from the devastations of Hurricane Mitch, the level of Bank approvals has provided clear evidence of the key role it is playing in containing the fallout from the turbulence in global financial markets. We believe that the Bank should focus a large part of its future efforts in these two areas.

The Bank must be active in preventing and mitigating the effects of natural disasters, so that the burden of risk can be distributed more appropriately among those countries that are best equipped to shoulder it.

On the other hand, while we have seen that markets are beginning to differentiate as to the quality and soundness of the economic fundamentals in individual countries, there is a need for the Bank to establish an incentive system that will recognize, support and reward the efforts of those countries that are pursuing sound economic policies but, because of the spillover effect, are facing market access problems. In this context, we believe the IDB should energetically promote the use of its guarantee program. It should as well engage in close coordination with the World Bank and the International Monetary Fund, to take a more active role in the work to develop a new architecture for the financial system. This initiative is inconceivable without the active presence of the IDB to guide and steer the effort. In this respect, Mexico gives its wholehearted support to the proposal made by the Governor for France to set up some kind of "Development Committee for Latin America" within the IDB.

In terms of concessional resources, we recently wrapped up what may well be the last replenishment of the Fund for Special Operations. The terms of that agreement are testimony to the deep sense of solidarity that unites the nations of Latin America with the less developed countries in their midst. I would like to invite our nonborrowing members to take an active part in giving substance to these common agreements of the Bank, by helping to close the FSO-8 funding gap, speeding up payments under previous replenishments and covering the contributions of the D-2 countries in the most recent resource increase.

Turning now to the Inter-American Investment Corporation, I am pleased that agreement has been reached to effect its long-awaited capital increase, so that the Corporation and the IDB itself become a solid presence as important sources of funding for the region's private sector.

Popular wisdom tells us that life begins at forty. That is surely the case as the IDB enters this new chapter, and we want to declare our fullest appreciation of the Bank's efforts on behalf of economic and social development in Latin America and the Caribbean.

First of all, allow me to join the previous speakers in extending my sincere appreciation to the Government of France and to the City of Paris for their warm hospitality and for the excellent arrangements provided for at the 40th Annual Meeting of the Inter-American Development Bank.

This Annual Meeting is a special occasion for the Bank. The Bank is celebrating forty years of successful operation and is at the same time on the wake of a new millennium. The Bank has during the 40 years transformed itself into a broad-based developing institution. It is now the largest multilateral development institution for Latin America and the Caribbean.

Before looking to the future, I would like to take a look back on the past year. A year with currency turmoil, with devastating hurricanes, and a year with a solution to the FSO.

Many countries in the region have already suffered because of the financial crisis, and there is a risk of further set back. The economic destabilization has lead to increased political and social challenges for Latin America. Denmark strongly supports the prompt reactions by both the countries of the region and the Bank to mitigate the crisis: The countries by implementing major fiscal and monetary measures, and the Bank by establishing an emergency lending program.

We see it as an extraordinary situation requiring extraordinary responses. Emergency lending is not a normal task for the IDB. Balance of payment loans are first of all an issue for the IMF. The present authority for the Bank to approve emergency loans is accordingly only granted for one year.

At the end of October the region witnessed one of its most severe natural disasters. Hurricane Mitch ravaged in just a few days large areas of Central America. The consequences were devastating, especially in Honduras and Nicaragua. Together with the international community and humanitarian relief organizations the Bank took swift action to mitigate the consequences of the disaster. We welcome this.

Ahead of us is an enormous challenge in rebuilding the infrastructure and the economic base of the countries hit by Hurricane Mitch. And a challenge to support the many poor whose bread and butter has been taken away. Furthermore, it is important to ensure that the rebuilding will be more resistant to new natural disasters than previously. Better early warning systems and contingency plans should, thus, be part of the rebuilding process.

Denmark only provides development assistance on a grant basis and targets its development assistance to the poorest countries in the world. Denmark therefore sincerely welcomes the conclusion of the FSO-negotiations. I would especially like to thank the regional countries for the solidarity they have shown reaching this historic agreement.

There is now an agreement on the concessional resources for many years to come. There is also an agreement on HIPC financing for Nicaragua and, if eligible, Honduras. The debt initiative contributes to a new start for countries willing to pursue a sound macro-economic policy. Denmark acknowledges the Bank's support to the HIPC-initiative. We support a decision on debt relief to Nicaragua and Honduras already in 1999. We encourage all donor countries to contribute by writing off bilateral debt and/or contribute to multilateral debt relief.

On the threshold of the 21st century, it is natural for all of us, including the Bank to look ahead. In Denmark's view the primary role of the IDB is to be a development institution with the overriding objective of fighting poverty. 35 percent of the region's population is still living in poverty. It is a much too high percentage.

To reduce this figure concerted efforts are needed. A broad economic growth policy has to be pursued. And particular attention has to be given to ensure a social and environmental sustainable policy.

Denmark notes with satisfaction that in 1998 the Bank adhered to the IDB-8 mandate regarding allocation of resources to the social sectors. It also approved new strategies in this area. Denmark trusts the Bank will continue to put special emphasis on social sector development in the future.

Popular participation in the development process is a precondition for sustainability. All citizens must be given an opportunity to participate actively in the economic and political development of the country. The Bank has been innovative in its approach to address these problems. One example is the pilot-project 'Social Policy Dialogue', which Denmark supports.

Denmark also commends the Bank for providing crucial support for modernization of the state and strengthening of civil society in the region. The preliminary work towards a strategy for cooperation with civil society has been undertaken. We look forward to its completion. There is a need for a clear definition of the concept and to find ways and means of strengthening and integrating civil society in Bank operations.

The importance of good governance for successful development is now generally recognized. The general principles have to be transformed into practical policies in the international development institutions. We would like to see the Bank play an active role in promoting good governance and supporting the establishment of communities founded on the rule of law and democratization. We encourage the Bank to enhance its work on policies in this area, including a policy on anti-corruption.

The UN Women's Commission is in these days planning the Special Session of the General Assembly in the year 2000. The Beijing Conference concluded that without equal participation of women a sustainable economic, social and democratic development cannot be ensured. This conclusion should be a guiding principle for all development institutions. Also the IDB.

We recognize the excellent work done by the WID-unit. But we also look forward to seeing substantial progress within the area of gender mainstreaming in the Bank's lending programs as well as in the Bank's institutional structures in the years to come.

Last year we extensively discussed a vision for the Bank. Following the FSO-agreement the discussions have, however, lost momentum. Denmark believes there is a need for a vision for the Bank's future actions. Fundamental questions regarding the overall role of the Bank need to be addressed, especially after the Bank has taken an important role in financial crisis and natural disasters. The vision should encompass both the Bank's relations vis-a-vis other multilateral development institutions as well as priorities in Bank operations. We hope the vision can soon be finalized.

Let me conclude by complimenting the Bank on the achievements that have been made in 1998 and indeed in its 40 years of operation. By its successful handling of both the economic crisis and the natural disasters, the Bank has shown its leading role in the region. Denmark wishes to pledge to you, President Iglesias, and to the Inter-American Development Bank our continued trust and support in the years to come.

I feel honored to attend this meeting of the Governors of the Inter-American Development Bank and Inter-American Investment Corporation, and wish to extend my thanks for the hospitality shown by the Government and people of France. Let me take this opportunity to congratulate the Bank's Management for its skillful administration, enabling the Bank to complete its fortieth year as a sound institution fostering development in the countries of the region and committed to the efforts of each and every one of our governments to alleviate poverty.

This is an excellent opportunity not only to assess the performance of the region's economies, but also to share a broad range of experiences and the concerns of our peoples about the region's future as we enter the new millennium.

For purposes of comparison, economic performance is best assessed on the basis of four indicators: stability, growth, employment, and income distribution.

In terms of stability, Bolivia's performance has been exceptional. From hyperinflation of more than 8,000 percent at the beginning of the 1980s, the rate had declined to barely 4.34 percent by the end of 1998, one of the region's lowest.

This was no accident. It reflects the political will of governments to maintain appropriate fiscal discipline with fiscal deficits declining continuously in recent years. Had it not been for the cost of comprehensive pension reform, in which the government undertook to change the pay-as-you-go system to one of individual pension accounts, the 1998 budget would have shown a slight surplus.

This result would not have been possible without the ability to steadily increase the tax ratio through a simpler tax system that has expanded the tax base and boosted fiscal revenue, with improved controls to minimize tax evasion. In 1998 the tax ratio, at around 18 percent, was among the highest in Latin America and the Caribbean.

In line with the report on inequality prepared by the Bank for this meeting, Bolivia recognizes that it is sometimes preferable to sacrifice tax progressiveness in order to ensure optimal collection levels, relying instead on social spending, particularly in education and health care, to serve as the mechanism for redistributing income.

It is precisely for this reason that we have participated actively in the HIPC program, which has not only helped reduce the burden of domestic debt on our budget, but has also freed budget resources for investment in the social sectors.

Because ours is a landlocked country, among other reasons, one of the most vulnerable sectors of our economy is road infrastructure. Although the Public Works Concession Act has now been passed, we believe the State should continue to participate in the construction and maintenance of most roads for some time to come. For this reason, road infrastructure financing by the multilateral institutions in general, and the IDB in particular, will continue to be essential.

The international crisis is forcing us to tighten fiscal discipline to counteract the deteriorating terms of trade for our commodities in international markets. This, combined with substantially rising imports of capital goods, explains the large current account deficit in our balance of payments, which amounted to 7.9 percent of GDP in 1998. Although a deficit of 7.2 percent has been projected for 1999, it is important to note that this deficit was entirely financed with foreign direct investment; thus, Bolivia's net international reserves remained constant at the equivalent of 6.5 months of imports.

Our managed float exchange rate policy is aimed at ensuring a single, competitive rate. It has also helped stabilize the level of net international reserves, which has in turn bolstered the confidence of international creditors and economic agents in the stability of the country's currency. The 5.21 percent devaluation of the currency in 1998 exceeded the rate of inflation.

Growth, though modest compared to the country's expectations, was 4.7 percent in 1998, more than double the average for the region, and for the first time in recent decades, was greater than the inflation rate recorded in the same period. It is estimated that growth in 1999 will be approximately 4.5 percent, with inflation of 5 percent.

This growth rate can be explained, to a great extent, by the high level of private investment in hydrocarbons, electric power, and agriculture. These sectors, however, are capital intensive, so employment quality and quantity have not increased as a result.

We recognize that rectifying inequality in our society will depend largely on creating more and better jobs. This means having the courage to modernize labor market regulations, but also supporting the growth of small and medium-sized enterprises.

In that regard we must stress the importance of the support we receive from the IDB in microcredit financing and technical assistance for small business. The financial depth of this sector in Bolivia is unquestionably among the region's greatest. The performance of microenterprise and small business in Bolivia offers clear potential as a significant means of formalizing the economy, and more importantly, creating jobs. Based on the financial performance of private microlending institutions, this is good business, and small entrepreneurs are creditworthy borrowers. The liquidity, solvency and profitability of Banco Sol, Bolivia's and the region's leading bank in the field of microcredit, are above average for traditional commercial banks.

In summary, Bolivia has managed to consolidate its monetary stability and achieve sustained growth—though still insufficient to address existing poverty levels. Our economic policy will continue to pursue economic growth with equity, in an environment of stability and employment opportunity.

We particularly wish to congratulate the Bank's Management for its report on inequality, which has helped us define more effective policies for reducing inequality in the region generally, and in Bolivia in particular.

The objective of our economic policy is consistent with President Banzer's program, which rests on four principles: *opportunity*, through economic growth and stability; *equity*, through better living conditions; a *sound institutional framework* for private sector activity; and last but not least, *dignity*, by taking Bolivia out of the coca/cocaine circuit under the current administration.

One of the keys to economic growth is investment. Bolivia has determined to limit State investment to sectors that are relatively unprofitable financially but yield a high social return, such as education and health care. In the production sectors, on the other hand, the government is leaving the field open to the private sector investment.

With respect to Bank strategies and policies, we applaud the IDB's approval in 1998 of 10 billion dollars in loans to borrowing countries in Latin America and the Caribbean, the highest amount ever approved in a single year. We would highlight both the regular lending program, which increased from US\$6 to US\$7.2 billion, and the special US\$2.85 billion program designed to help the countries weather the global financial crisis. It ought to be a matter of pride for the Governors that the Inter-American Development Bank, for the fifth consecutive year, is the region's premier multilateral development bank.

As Governor for one of the FSO beneficiary countries, I wish to express our appreciation to the Bank, and especially to the countries that made available local currency deposits at in their central banks to finance the concessional resources lending program for the next 10 years in total amounts of 2 billion dollars for 2000-2003 and 2.4 billion dollars for 2004-2009.

These amounts, however, are not sufficient to meet the development needs of the least developed, Group D-2 countries, and although we understand the difficulties entailed in financing a greater amount, we hope that a new increase in resources for the FSO window can be negotiated in the near future. Although the current solution does not include new contributions from the nonborrowing countries, their commitment to reducing poverty in the region is clear.

We believe the Bank should continue to place emphasis on financing social programs, which last year, according to the reports, accounted for 46 percent of all projects approved.

We wish to call special attention to the breakdown of operations by country group, since the share of Group C and D countries fell to 30.2 percent, as compared with the indicative target of 35 percent under Bank policy.

We also wish to express our full support for the Action Plan to strengthen the Country Offices and the Action Plan for Group C and D countries, which have proven valuable tools for enabling Country Offices to respond rapidly to requests for assistance and finance consultancies in specific cases.

We firmly support as well the new Social Entrepreneurship Program, known earlier as the Small Projects Program. We are convinced that the proposed program will expand opportunities for microentrepreneurs by embracing small production and social development projects as generators of much needed employment in our countries.

We urge Bank Management to do its utmost to increase cofinancing from bilateral sources for the nonreimbursable technical cooperation program.

Now that fewer funds are available for this program, we consider the donor trust funds an essential source of resources and specialized expertise for project design and preparation, offering assistance to strengthen local institutional and administrative capacity.

We also welcome the introduction of guarantees and diversification in the Bank's private sector portfolio, as well as the increase in the number of group C and D country operations.

We agree that the Bank should lend to the private sector up to 5 percent of the balance outstanding on authorized loans, thereby expanding this program by 600 million dollars annually over the next three years.

Also important for our country is the Bank's private sector strategy, whose aim is to improve key aspects of the business climate and which is becoming a fundamental tool for designing the lending program and country-Bank dialogue.

To conclude, I wish again to convey my country's appreciation for the work performed by the Inter-American Development Bank toward regional development in general and the development of Bolivia in particular.

On behalf of the Swiss delegation, I should like first to thank our hosts, the French people and government, for the warm welcome we have received here in Paris. I should also like to express my appreciation to the President and staff of the Bank for the quality of the documents distributed for this annual meeting of the Board of Governors.

The financial shocks and natural disasters that have struck Latin America recently place a heavy burden on the people of the region. I wish to express Switzerland's solidarity with the governments and peoples so suddenly and cruelly thrust into these crises. Like other speakers before me, I also take this opportunity to tell President Iglesias and the Bank's staff that we appreciate the Bank's swift and effective action during these difficult times.

The economies of Latin America and the Caribbean are now suffering the repercussions of global financial instability. The negative impact on growth, employment, and living conditions has been extremely high. Nonetheless, it is clear that—thanks to their legitimate democratic governments and open economies—countries in the region have successfully contained the most harmful effects of the financial crisis. This gives us reason for optimism that the emerging economies of Latin America and the Caribbean may soon regain their place as important centers of economic growth.

This is particularly true in that several initiatives have recently been announced to support the reconstruction of Central America and lighten the debt burden of poor countries. I commend these efforts. Switzerland has already mobilized substantial resources for international action to assist populations affected by Hurricane Mitch. We will be taking part in the next Consultative Group meeting in Stockholm, where I expect the IDB, in close cooperation with the authorities concerned, will undertake to ensure the best and most effective use of funds. With respect to poor country debt, Switzerland encourages its partners, and in particular the G-7 countries, to take the courageous and decisive measures called for. More than 20 years ago, the Swiss government canceled all concessional public debt. Since 1992, we have also forgiven bilateral commercial debts owed by 19 poor countries; and we are contributing US\$30 million to the trust fund for the Highly Indebted Poor Countries initiative.

The Bank has provided substantial emergency financial support to the economies affected by the crisis. I fully understand the particular circumstances of these operations, and I approve of the decisions taken. Nonetheless, the time has come to better define the role and mandate of the Bretton Woods institutions and the regional development banks, as well as possible private sector participation in response to these crises. It is in that spirit that Switzerland is approaching the discussions on the new architecture of the international financial system. I hope that in the next few months the Bank will establish a precise definition of the framework and nature of its emergency financial operations.

The massive commitments undertaken recently by the IDB in connection with this type of emergency operation have had a significant impact on its financial position. The risks associated with increased geographic concentration, the effects on the Bank's prudential ratios: all of these elements call for careful management. In an increasingly fragile financial system, our Bank must remain a pillar of solidity and credibility. The IDB must also continue to be particularly attentive to the needs of the poorest countries.

Against this backdrop, Switzerland welcomes the agreement concluded last December on concessional resources, an agreement that also touches on the question of financing debt forgiveness under the Highly Indebted Poor Countries initiative. We recognize the efforts and display of solidarity on the part of all the Bank's members and believe the IDB now has the financial means necessary to pursue its course of action and to coordinate and mobilize through and leverage substantial cofinancing for its priority programs and projects.

Switzerland has been an active member of the Inter-American Investment Corporation since its inception. The reason is simple. Mobilizing private resources, fostering the entrepreneurial spirit, promoting private investment—particularly for small and medium-sized enterprises—are objectives and approaches which have for years been at the center of Switzerland's policy of economic cooperation with emerging economies. Our relationship with the Inter-American Investment Corporation is based on this combination of analysis and strategy.

We have long shared the view that an increase in capital is indispensable to strengthen the financial foundation of the Corporation. Our firm support for this capitalization exercise enables me to view the current negotiation process somewhat critically.

It is indeed clear that despite a favorable context—broad support for an increase in capital, openness to new membership, and the interest of several prospective members—we have not made significant progress. Conflicts of interest, excessive claims and inflexibility have affected the negotiations. It is my hope that all members of the Corporation will adhere to the timetable currently being proposed so that it will be strictly respected and provide the opportunity for a better structured and more effective negotiation process. With calm restored, I also hope that all members of the Corporation and the potential new members can once again consider themselves full partners in and parties to these negotiations.

Together, we must now all concentrate on the significant challenges facing the Corporation. These challenges are considerable, given to the exceptional increase in capital now being envisaged. Faced with these challenges, we believe the "Blueprint 2000" paper articulates a certain number of important strategies. In the weeks ahead, we expect to see the Corporation's Board of Executive Directors engaged in an intensive effort with respect to managerial methods, institutional capacities, and strategic, financial, and operational approaches.

More than ever before, the Inter-American Development Bank faces important and diverse challenges and expectations. Accordingly, to avoid doing more but not necessarily better, the Bank must redefine its strategic framework for the years ahead. It is essential to optimize the allocation of resources to certain priority areas of activity. While our institution must maintain the resources needed to serve as a laboratory and clearinghouse for new ideas, it must also focus its efforts on strong and determined action within its fields of excellence and in areas where it enjoys a comparative advantage. We see evidence of those areas every day.

At the dawn of a new millennium, the Bank's future should, in my view, develop along two major axes. On the one hand, for the poorest countries of Latin America and the Caribbean, the Bank should continue to play its lead role as a coordinator and catalyst of multilateral resources in support of lasting economic development and the fight against poverty. On the other hand, for the emerging economies, the Bank's role should evolve more dramatically. Rather than financing programs and projects directly, it should increasingly devote itself to providing knowledge and expertise, as well as the leverage needed to mobilize private resources. Such a shift calls for the Bank, first of all, to examine options for funding technical assistance, which may no longer be granted in the form of grants alone. Also, an effort ought to be made to bring the private sector into a true association with this process, and therefore included in our deliberations. We welcome France's proposal that an IDB Development Committee be set up. Giving the private sector a seat on such a committee would make it a full partner with the Bank.

This process of change should be combined with an ongoing effort to improve the Bank's management practices and procedures, to promote greater efficiency, transparency, and accountability, and to increase the impact of its operations on development in the member countries. In that regard, I commend the efforts being deployed in developing the new corporate strategy and encourage management to complete this process as soon as possible.

I am honored once again to address the Board of Governors of the IDB as we meet on this occasion in Paris, France. This is the sixth consecutive year I have had this privilege, making me the longest standing Latin American governor and one of the three governors here today who have continued in office since the Eighth Replenishment in 1994.

This is a special occasion for me, not only because we are gathering in this historic city, but also because I had the honor yesterday of accompanying the President of Chile, Eduardo Frei, as he personally extended the greetings of the people and the Government of Chile to the esteemed people of France, to the Inter-American Development Bank, and to all the special guests who are joining us on this occasion. I should like to extend these greetings once again today. I should also like to take this opportunity to express our deep appreciation to the President of the Bank, Mr. Enrique V. Iglesias, who, once again, has guided the IDB through a difficult period in the region. I greet the new Executive Vice President, Ms. K. Burke Dillon, who has made the transition from the Anglo-Saxon restraint of the IMF to the spirited world of Latin America as it looks optimistically to the future.

The context in which we are meeting is quite different from that of the last five years. The international financial crisis that originated in Asia hit the region hard and unfairly, requiring adjustments and sacrifices in all our countries. We were looking forward to 1998 as a year when the advances achieved through great effort and discipline in Latin America and the Caribbean would be consolidated, but it ended up being a year of bad tidings. The region's economic growth, which averaged 3.7 percent from 1994 to 1997, fell to almost zero in 1999.

This unfavorable situation affected Chile, as well. The openness of our economy meant that we were one of the first countries to feel the impact of the crisis. Of the countries of Latin America, Chile has the greatest access to the markets of Southeast Asia, and the value of our exports to the region decreased 33 percent in 1998 in consequence of the region's difficulties. Moreover, since late 1997 Chile has suffered a sharp decline in its terms of trade which, by itself, represents a loss estimated to amount to three percent of output. Thus, of the countries in the region, Chile suffered the greatest shock to its balance of trade.

In other circumstances, the impact of this crisis would have had a devastating effect on the Chilean economy. Absent the multiplying factor added on this occasion by the volatility of private flows of capital, Chile suffered deep recessions in 1975 and 1992 when faced with decreases in the terms of trade that were less drastic than those of this past year. However, the prudence and discipline of our long-term policies during the past decade enabled us to weather the effects of the current international crisis quickly and effectively, limiting the contagion effect on the Chilean economy.

In fact, during the 1990s, not only did Chile experience vigorous growth, reducing poverty and inflation, but it strengthened its economy to prevent the volatility that produced such great damage in the past. This meant diversifying our trade, maintaining sustained budget surpluses, establishing the copper fund, developing a strict system of bank oversight, building up international reserves, and discouraging the entry of short-term capital. As an outcome of this strategy, Chile managed to cope with this crisis without the pressures of short-term debt maturities, without the risk that interest rate hikes would add to the budget deficit or do harm to the financial system, and without having budget adjustments paralyze our program of reforms and social progress. In other words, the responsible actions taken in previous years gave the economic authorities the freedom they needed to respond quickly and effectively to the unfavorable external economic situation.

Our response to the crisis was fast and multifaceted. To control the growing current account deficit caused by external factors, domestic spending had to be adjusted radically. To achieve this, we relied on a mix of cuts in public spending, a restrictive monetary policy, and a moderate and orderly depreciation in the exchange rate. As a consequence of the combined effect of these policies, domestic demand fell from an annualized growth rate of 15 percent in the first quarter of 1998 to a 10 percent decline in the fourth quarter. This drastic contraction in demand allowed us to reduce the balance of payments current account deficit from 8 percent of GDP in the third quarter to 6.2 percent in the following quarter. For 1999, it is estimated that the current account deficit will be on the order of 4.5 percent of GDP.

Despite coping with an external shock that was even greater than that experienced by most of the region's economies, Chile achieved 3.3 percent growth in GDP in 1998, reduced inflation to 3.7 percent (the lowest level in 60 years), and maintained investment at approximately 30 percent of GDP. Although the figures for 1999 will reflect the impact of the concentration of adjustments in the second half of last year, as well as the delayed effects on employment, the economy will grow once again in 1999 at a rate of approximately 3 percent.

However, as important as it was to carry out effective adjustments in the face of the international crisis, it was equally important to do so without jeopardizing our long-term policies.

The government of President Frei has focused its efforts on three strategic areas in order to maintain long-term growth and to ensure that all sectors benefit from it. To that end, we implemented an extensive program of infrastructure concessions, involvement of the private sector in managing water-supply companies and ports, thoroughgoing reforms in education and the administration of justice, and modernizing and decentralizing the State. None of these programs is at risk in the aftermath of the international crisis and budget adjustments. This past year, not only did Chile overcome external shocks but it continued to post progress in terms of the transformations needed to take development to the next level.

Therefore, the conclusion that we draw from this very difficult phase is a reaffirmation of the choices that Chile made in previous years. When the country's authorities and key economic players act responsibly, they must be able to count on more, not fewer, policy instruments; using these instruments is a sign of strength, not weakness. In like manner, this strength is better demonstrated in the ability to balance short-term and long-term goals than in the dominance of one group over another.

We believe that many outside observers understood these factors, which explains why, during such a difficult period for emerging economies, Chile has maintained its credit rating, attracted more than US\$6 billion in investments in 1998, and saw capital resources competing to invest in Chilean companies.

In recent years, far from standing apart, Chile has strengthened its ties with Latin America and the Caribbean. At present, Chile has associate member status with MERCOSUR, and has free-trade agreements with nearly every other country in the region. Chile welcomed the leaders of the Americas at the Second Summit of the Americas in Santiago, and is now one of the countries responsible for implementing the agreements reached on that occasion. We are deeply involved in efforts to strengthen bank oversight and in the FTAA negotiations. We are concerned about the future of Latin America and the Caribbean, since that is where our roots and where many keys to our future lie. Integration has gone from being a dream to being a necessity. In today's increasingly global world, no country can be sufficient unto itself, no matter how determined and responsible it may be. Still, integration is easier with those to whom we are united through a shared history and culture.

The future of Latin America and the Caribbean holds great challenges for each of our countries, and for the IDB. This may well be the part of the developing world where first-generation reforms and internal economic adjustments have been pursued with the greatest determination. However, the advances we have achieved and the prospects for the economic future mean that we must ask ourselves what we want the future fundamental nature and appearance of the region to be.

We have tried to be a disciplined and realistic region in the face of macroeconomic realities, leaving behind a past marked by risk-taking, protectionism, and political volatility. While authoritarian regimes still hold sway in other regions, the political leaders of Latin America have demonstrated their courage and their ability to make difficult decisions and to push ahead with far-reaching reforms without having recourse to arms. Today, we are a region of peace and democracy. We are taking fundamental steps toward integration.

However, we are also a region of great inequalities and institutional weaknesses. The most recent annual report of the IDB notes that our region has the greatest inequality in the distribution of wealth in the world, and that our development in terms of education is lagging dangerously behind. Similarly, recent studies by the World Bank point to significant institutional weaknesses. All these factors limit the long-term competitiveness and development potential of Latin America and the Caribbean.

Now is the time to take the initiative to meet these challenges. We must draw on our strengths in order to deal with our weaknesses. To do this, we need the support of multilateral organizations that are able to listen to, understand, and represent our interests.

The IDB holds pride of place in this respect, not merely because of its historical regional identity, but also because the concept of development that is taking shape for Latin America and the Caribbean is in large measure reflected in the agreements of the Eighth Replenishment: socially balanced development that favors integration and is sustainable. However, the IDB needs much more than history, mandates, and sheer will in order to play an effective role in this process. The IDB must reflect its commitment to the region's development in every decision, every procedure and every project, and must be organized in such a way that it can carry through on this commitment.

We are convinced that the current strategic planning process is headed in exactly this direction, transforming the IDB into a reliable and effective partner in the region's development endeavors. However, this commitment requires more policy signals on the part of the IDB and those of us who are its members. Key among these signals is the Bank's willingness to listen to and respond to the needs of each country in the region, adapting its set of instruments to suit the differing conditions in each country. If the IDB is to adequately represent the shared interests of the region, it needs to intensify its dialogue with each of region's countries, respond to our various needs, and listen to all when it comes to making institutional decisions.

It is because those of us here today know each other, and are aware of how important it is for the Bank to continue to be the instrument for development that its founders hoped it would be, that I believe we can speak frankly: we are concerned about the way in which the problem of concessional resources was settled recently. We are concerned that these decisions have tended to favor the emergencies, interests, and limitations of a few countries over the tradition of consensus that has been characteristic of the Bank. We are concerned that the borrowing countries have had to shoulder all the costs of the solution at the very moment they are facing drastic adjustments, while many of the nonborrowing countries are enjoying robust growth.

We voted in favor of the solution as an expression of our loyalty to this institution. We support President Iglesias in the difficult task of implementing this solution. However, our position does not reflect a lack of concern with the impact of these decisions on the IDB's ability to carry out its priorities, to respond flexibly to the various needs of the region, and to fulfill its commitments to member countries.

Just a year ago, the IDB was present at the Second Summit of the Americas in Santiago, and it became aware of the priorities of the hemisphere's leaders as expressed in an action plan whose implementation depends substantially on the Bank's support. Nonetheless, today we know that the limits on the capacity to make regular loans in 1999, the restrictions on disbursements, and the drastic reduction in technical-cooperation resources may jeopardize fulfillment of the principal commitment assumed by the IDB to support efforts to increase greatly the quality and equity of education.

The manner in which the discussion on concessional resources was conducted and brought to a conclusion, however, stands in contrast to the great degree of consensus among all the Bank's member countries regarding the development priorities and strategy that the region needs. Historically, it is such consensus that has brought about major advances in the development of the IDB. This is not the time for small-minded disputes but for promoting broad-based agreements on the directions for future actions by the Bank, and to commit ourselves to following them. This is the time for promoting confidence among the member countries represented at this meeting.

One of the likely causes of the problems that have surrounded recent discussions among the member countries of the IDB is that the discussions have taken place outside the framework in which the overarching themes and institutional priorities can be resolved: capital replenishments. As a participant in the 1994 Guadalajara meeting, I can bear witness that the capital replenishments were an occasion to provide the Bank with new resources and, above all, to hold a frank dialogue on its future priorities, a dialogue in which we all had the right to speak and to be heard.

I believe that it is essential for us to regain that forum and that spirit. The fact that increases in the Bank's ordinary capital are not on the horizon does not mean that we should lose the opportunity to hold an open and pluralistic dialogue in which we can evaluate the IDB's performance, identify new priorities, and equip the institution to deal with them.

Therefore I believe that we must take the initiative to regain the spirit of the capital replenishments. Specifically, I believe that we should entertain the idea that in two years, the IDB should devote its annual meeting to conducting a general review of its performance, its policies, and its priorities, resolving the institutional problems that must be addressed in order to ensure the organization's vitality. This discussion must be accompanied by the agreements needed to provide the IDB with resources that are separate from the ordinary capital it requires for implementing these new priorities, including those relating to technical cooperation.

The two-year period for accomplishing this review will give us enough time to do the preliminary work and prepare the studies and budgets that will be needed for a frank and well grounded discussion, and to overcome the economic circumstances that gave rise to and that derive from the recent agreements on emergency loans and concessional resources. This two-year period should not delay decisions on corporate strategy and human resources, procedures, and evaluation. Rather, it will give them enough time to be implemented, increasing the IDB's effectiveness in carrying out the mandates that make the Bank a key player in building the Latin America and Caribbean of the twenty-first century.

Just as Chile was present at the establishment of the IDB and at each of the capital replenishments, just as it worked with the Bank in designing innovative programs, and just as it is, even today, involved in laying out the Bank's new institutional strategy, Chile is also prepared to engage in an effort of this kind.

Because we are part of Latin America, because its future is our future, because we cherish this Bank and have confidence in its President, Chile is prepared to offer its strong support for efforts to strengthen the Bank, with which we have formed a bond through these many years of friendship and cooperation.

Allow me first of all to join previous speakers in expressing my sincere appreciation to our generous hosts from the Government of France and a special thanks to President Iglesias and the IDB staff. I would also like to welcome the new Vice President Burke Dillon.

The past year has been a particularly strenuous year for Latin America and the Caribbean, and also for the Inter-American Development Bank, due to the consequences of the international financial crises and the natural disasters that hit the region. The natural disasters (Hurricanes George and Mitch, earthquakes) have had an enormous negative impact and it will take a long time until the region has recovered. At the same time, we have to look ahead and identify ways to move forward.

The 1990s have on the whole been a good decade in Latin America. We have witnessed several heartening successes on the continent. The newly established democracies are gradually being consolidated. Armed conflicts and great power intervention in Central America have ceased. The power of the military, previously so great, has diminished. The economy has been growing and inflation has gone down. The previous isolation has been broken, and instead regional cooperation has been revitalized and foreign trade is finally being liberalized, which has led to both increased trade and growing private investment.

The steady expansion in Latin America's economy during the last decade is however set to come to an abrupt halt this year. Recession is expected to lead to a contraction in the continent's gross domestic product for the first time since 1990.

There are also other clouds over the Latin American continent. Latin America has the most skewed income distribution in the world. As the latest report of IDB's *Economic and Social Progress in Latin America (1998-1999)* notes, it is not improving.

As Amartya Sen so clearly expressed a couple of days ago at one of the seminars of this meeting, development and reduced poverty gives greater freedom of choice. The abject poverty in which over 200 million Latin Americans live is the greatest obstacle to the consolidation of democracy in the region. As long as millions of people see no hope of a better future, their confidence in democracy will remain low. Thus, measures to achieve equitable sustainable development are urgently needed.

As evidenced by events during the last year, both on the global scene and in Latin America, the coming decade will be crucial for the ambitious reform agenda that the Latin American and Caribbean countries have set up for themselves. We are glad that we can count on such a vigorous partner in this endeavor as the Inter-American Development Bank.

The Bank is the biggest source of multilateral financing to the region and, as envisaged in the mandate provided by the Eighth Replenishment, the major objectives of its activities are poverty reduction, social equity, modernization of the State and environmental sustainability. In this context, Sweden would particularly like to encourage the Bank to continue its efforts to effectively implement the poverty-reduction strategy, the mainstreaming of gender in all parts of the Bank's operation, and promoting democratic development and human rights issues.

Based on its closeness to the region, we believe that the IDB has a unique opportunity to further strengthen its role as a regional promoter for important issues such as vulnerable groups (women, children and indigenous people), practices of good governance, anti-corruption measures, decentralization and local development. Sweden in particular welcomes the increased attention given by the Bank to the role of local governments in the region.

The major objectives of the Bank and the new focus areas are well in line with Swedish priorities for international development cooperation. Sweden is looking forward to an expanded and innovative cooperation and exchange of experience on these issues in the future, as evidenced by the pending formalization of a partnership between the Bank and the Swedish International Development Cooperation Agency, Sida/Asdi.

The concessional lending of the Bank to the poorest countries in the region is an important instrument for poverty reduction. We are very pleased that a long-term solution for financing the Bank's concessional resources, which also ensure the IDB's continued participation in the HIPC initiative, was agreed upon late last year. We especially appreciate the solidarity and commitment of the regional countries, which was key to the success.

Sweden welcomes the ongoing work to develop a medium-term corporate strategy, aimed at strengthening the capacity and efficiency of the IDB. We also welcome the development of a human resource strategy as a complement to this plan. This should ensure staff rotation, the creation of incentive structures, the continuation of the work to establish an adequate skills-mix between headquarters and country offices, with a particular focus on strengthening the country offices.

At the same time, it is important to continue the visionary discussion about the long-term future role of the Bank. We believe that the IDB has a role to play not only as a central poverty-oriented development institution in Latin America and the Caribbean, but also as an important actor in an improved structure for global governance. As emphasized by the effects of the financial crises, there is a need for close cooperation between the multilateral financial institutions. The latest rescue package for Brazil is a good example of this. It is therefore important for the IDB and the other regional development banks to take part in the ongoing discussion of a new international financial architecture.

It is also important to deepen and find new avenues of cooperation with the UN system, especially at the field level and in the programming process. Only then can the true potential of the multilateral system be effectively utilized. It is also crucial to create forms of cooperation and partnerships with other actors, not least civil society. Therefore, we urge the Bank to give priority to the development of a strategy on the strengthening of civil society.

As a result of altered patterns of financing, together with rapid changes in the global political and economic environment, we see an emerging development where policy dialogue, dissemination of knowledge and good practices as well as capacity-building are becoming as important a part of the Bank's activities as the channeling of financial resources. As one way to strengthen the role of the IDB in policy dialogue, Sweden welcomes the idea to create a new forum where strategic policy issues can be discussed at the Governors' level. Such a forum should facilitate making the Latin American and Caribbean voice heard and foster partnerships.

Another important role for the IDB is to facilitate the transfer of private capital to the region. The financial crises have underlined the need for this catalytic role.

Concerning the private sector activities, important discussions have taken place during the last year on strengthening the Inter-American Investment Corporation. We welcome the agreement now reached on expanding the capital base of the Corporation, but regret that there was no final conclusion regarding the conditions for accession of new members, including Sweden.

I will end with only a few words on the disaster that hit Central America last year, killing thousands and ruining the livelihood of so many more. After years of painstaking effort by the Central American societies to build a prosperous and integrated future, the devastating hurricane was the last thing they needed. We must all join in to help Honduras, Nicaragua, El Salvador, Guatemala and their neighbors rebuild their countries, transform their societies and integrate the region. We must use this opportunity not just to rebuild the old, but to shape something new. We need to build political momentum for increased cooperation and coordination, and pledge strong commitments for coherent action towards the transformation of Central America. This means reducing social inequalities and ecological vulnerability, strengthening the mechanism for decentralization, broadening participation and firmly establishing the principle of transparency. We need to strengthen the partnerships with NGOs, the private sector and other parts of civil society.

Since many of us met in Washington in the immediate aftermath of the disaster, support is becoming more concrete. We know from experience that it is extremely important how we shape our partnerships and pool our efforts. The Consultative Group meeting on the Reconstruction and Transformation of Central America, to be held in Stockholm in May in just nine weeks, should now be our focus. We are honored as hosts to work closely with President Iglesias and his staff to ensure that the outcome meets all our expectations.

The Central American countries need to present their plans for reconstruction and transformation. Partners need to respond through substantial pledges. And we need to work out ways to follow up on this partnership. If we put our minds to it, we can give this partnership a new quality. A declaration by all to this effect would set a new partnership standard.

Let us therefore use the best of our abilities to work together in the coming months and years to support the people of Central America, and the advances they hope to achieve, just as we did after the Central American peace agreement ten years ago.

As the representative of the State of Israel, I am pleased to have this opportunity to address the Fortieth Annual Meeting of the Inter-American Development Bank and Fourteenth Annual Meeting of the Inter-American Investment Corporation.

I would like to start off by welcoming the new Vice President, Ms. Burke Dillon. I would also like to express my gratitude to the French authorities and the city of Paris for the warm reception and for the superb organization of this event.

It was here in Paris, some 200 years ago, that the principles of liberty and equality were proclaimed. While these principles are now accepted without question, they are unfortunately not yet practiced throughout the entire world. It is true, however, that where equality and individual freedom do not yet hold sway, this may well be the legacy of ineffectual social policies rather than an indication of totalitarianism.

Obviously, this does not make the situation any more acceptable. Recently, the international financial institutions (IFIs) made it an objective to help change such social conditions by building this aim into their economic-advancement mandate. This new approach to the role of the IFIs was embodied in the mandate for the Bank's Eighth Replenishment. The Bank, under the forward-looking stewardship of President Iglesias, recognized that it had a responsibility to become actively involved in fostering socioeconomic equality as well as strengthening civil society.

In 1998, the region was buffeted by the global financial crisis and a succession of natural disasters, which left it more vulnerable to external shocks, which the frequent natural disasters in turn compounded.

After these introductory remarks, I shall switch to a language in which I am somewhat more adept than in French.

In the wake of the August 1998 crisis, most emerging markets in the world lost much of their access to external financing, even those economies that did not present great inherent weaknesses. The drying up of financial flows occurred at a time when terms of trade for the economies of the Region were deteriorating. Thus, while current account deficits were widening because of the deterioration of terms of trade, their financing has become increasingly difficult because of the drying up of financial flows. Brazil has been the main victim of this change of tide as fiscal imbalances have been brought to the surface and forced a sharp devaluation of the real. While a panic in international financial markets has been averted, the impact of this crisis on the Region could be significant. Apart from the possibility of contagion being sparked off in other economies of the Region, the crisis in Brazil is bound to have repercussions on its trading partners and in particular on the other members of MERCOSUR. The Region, in general, now faces serious risks of a loss of investor confidence. In recent years private capital has been playing an increasing role in investments. If, because of loss of confidence, private capital becomes scarce, development in the Region will suffer further repercussions from the present crisis.

The Region seems to be predestined to natural disasters; it certainly had to bear more than its fair share of them in 1998. The year was marked by the devastating effects of El Niño, by Hurricane Georges which caused havoc in the Caribbean and, worse still, by Hurricane Mitch which swept through Honduras, Nicaragua, El Salvador and Guatemala, leaving in its wake death and destruction. The capacity of the respective governments to respond in the face of these disasters has been reduced both by the increased expenditure required to deal with the most urgent needs and by the decrease in tax revenues occasioned by the drop in production. This situation poses major challenges with regards to institution building and fiscal administration in the poorer countries of the Region. These events emphasize the need to strengthen systems for fast response in emergencies, in those countries of the Region, which are prone to natural disasters. Physical and economic infrastructure should be reinforced in order to become less vulnerable to such disasters and at the same time enable a faster recovery time from them.

Ironically the adversities that hit the Region brought about the resolution of the long-standing issue of concessional resources. In a historic decision, the borrowing countries agreed to the conversion of over \$2 billion of their local currency contribution to be used in the concessional lending program for the poorer countries and to help reduce the debt service burdens of Nicaragua and possibly Honduras under the HIPC initiative. In 1998 the Bank's operations totaled an unprecedented figure of over \$10 billion. Two factors explain this record in the Bank's lending history: (i) the growth in the Bank's regular program which went from 6 billion to \$7.2 billion and (ii) the establishment of a special lending facility to provide financial support in the wake of the global financial crisis, which accounts for the rest. Let me just say that while the Bank's involvement in the emergency lending programs for countries affected by the global financial crisis has been inevitable, this should be considered only as a temporary deviation from its long-term development mandate.

It is the poorest sectors of the population who are the principal victims of the economic volatility and of the frequency of natural disasters in the Region. For example, in the wake of the "tequila crisis" four years ago some 9% of the young abandoned their studies in order to seek early entry into the labor force, and many over the age of 55, who were still professionally active, were forced into early retirement. These effects were not reversed by the subsequent recovery of the Mexican economy - the end result being a huge loss in human capital and social progress. It is too early to assess the repercussions of the present financial crisis on the poor. Invariably, it is the poor who are also the most vulnerable to natural catastrophes, as shown by the tragic toll of Hurricane Mitch. Thus the effect of these shocks is to increase an already high rate of inequality which exists in many countries of the Region. The present report of the Chief Economist "Facing Up to Inequality in Latin America" addresses this subject.

As the Introduction of the Report mentions, it is not that the governments of the Region have been oblivious to the problem, but rather that their attempts to solve it were wrongly targeted and ineffective.

One important factor, which is both the cause and the result of this inequality, is education. For one of the most evident causes of inequality is the lack of skills of the poor, preventing them from reaching an adequate level of income. This is a self-perpetuating problem transmitted from one generation to the next. One of the top priorities on the agenda of the governments of the Region, as well as of the IDB, should be the upgrading and improvement of the quality of education. In the case of Latin America the problem is not the lack of schools, but the inadequate quality of public education and the high dropout rate. This is an area in which the IDB's contribution could be intensified: in 1998 only five projects were approved in the education sector (for a total amount of \$293 million), representing just 4% of total lending.

Improvements in education have their largest influence on income and inequality in the medium and long term. This can be done by improving the supply of quality education through institutional reforms and by increasing the demand for it through improved quality and reduced costs. In my own country, Israel, which has hardly any natural resources, investment in human capital has been recognized as the way forward, and we owe our well developed high-technology sector to the availability of the appropriate human capital. The development of the industrial sector in Latin America should not be led by the availability of a low-wage labor force. As we know well, foreign investments are drawn by a number of factors, such as liberal economic policies, political and social stability, but not least by the availability of an educated labor force.

During the four decades of the Bank's operations, great changes have taken place in the Region. Democracy has been restored or established in all the regional borrowing countries, regional integration has strengthened and inflation, which has afflicted the economies of Latin America in the past, is no longer a threatening concern. Furthermore, most of Latin America stands at an opportune moment in its demographic transition, with fewer children to care for than in the past and still relatively few old people to sustain. As the Chief Economist's Report points out, the present generation of Latin Americans is in a position to be an engine for economic growth and social change. During its years of operation, the Bank itself has also evolved and matured. Public sector lending for infrastructure projects is no longer its principal objective. It has recognized, at an early stage, the importance of a viable and competitive private sector in establishing the IIC in 1986, and more recently it broke new ground with the creation of the Private Sector Department. The political and social climate of the Region today, as well as the demographic trends and the present institutional capacity of the Bank, offer opportunities for the deepening and widening of reforms so that its further development will not be handicapped or inhibited by its vulnerability to external shocks. In this respect, I was very much encouraged to hear the initial reflections on the road ahead that President Iglesias presented at the meeting of the Committee of the Board of Governors last Sunday.

It gives me great pleasure to be present here today and to address this distinguished audience. First of all, I would like to express my appreciation to the City of Paris and the French government for the generous hospitality they have shown us while hosting this annual meeting.

Allow me also to express my sympathy for the countries and people who became victims of the vicious Hurricane Mitch last year. This natural disaster has brought human suffering, increasing difficulties and shortages for the region affected. Finland participates in the efforts of the international community to mitigate the suffering and to reconstruct the region.

At the beginning of last year, the economic prospects for Latin America seemed rather promising, due to extensive structural and sectoral adjustment programmes aimed at reforming economic policies and management, and determinedly carried out by the countries in the region. At the end of the year, however, the international financial crisis had reached Latin America, requiring immediate and effective action. Financial turmoil affected both small and very large economies. The IDB participated commendably in the efforts to promptly and committedly mitigate the impact of the financial crisis together with other international financing institutions.

At the same time, the Bank launched an initiative leading to an agreement on its role in emergency financing. Regional institutions like the IDB have a responsibility to assist countries suffering from direct or indirect effects of the financial crisis. But it is of crucial importance to have a common understanding on the IDB's role in emergency lending. The participation in an emergency context must not endanger the Bank's primary role as a long-term development financing institution.

After having addressed the immediate effects and impacts of the crisis, the time has come to consider the causes and factors behind unstable financial conditions. The crises in Latin America and Asia have shown that sustainable economic development and financial stability cannot be established without political stability. This, in turn, is based on the principles of democracy, respect for human rights, social justice, the rule of law and good governance. To reach these goals, factors of ethics and morale need to be applied. Corruption, inequality and uneven distribution of wealth are a potential threat to stability and development.

Globalization offers a powerful vision for wealth and development. But these are impossible to achieve when the State is not in a position to apply the necessary values. Global governance is needed because market forces alone are not sufficient to bring about sustainable development. The major international organisations have been challenged to redefine their work in the service of the common political will of the international community as an effective governance mechanism. Coherent action and a new kind of cooperation demand long-term values to be common. It is obvious that a new international financial architecture is needed. The IDB and other financial institutions need to participate actively in formulating the necessary framework to define and implement their role in this new structure. The Bank is to be commended for launching the debate on its future role in this new environment.

Development-financing institutions are facing the challenge to continue work on financial policy reforms and capacity-building for sound economic management simultaneously with the development of sustainable social services and social equality. The Inter-American Development Bank has come a long way in successfully responding to this challenge. But additional efforts from both the Bank and from Latin American governments are being called for to address these issues.

Last year the Bank faced the difficult task of finding a long-term solution to the reduced resources of the Fund for Special Operations in order to ensure a continued and sufficient response to the financing needs of the poorest countries. The important agreement reached on the concessional resources in December last year and the Bank's efforts in looking for a solution are signs of its strong commitment to fulfill its mandate in the poorest countries.

Cooperation between Finland and Latin America has diversified in recent years. Previously, Finnish relations with the Latin American countries had been characterized mainly by bilateral development cooperation and trade in primary agricultural products. Now, the focus of relations is increasingly extending to cover political relations and to include more diverse economic and trade ties. Our partnership with the IDB has played a significant role in this development.

With growing interest in the Latin American region and having noted the growing importance of the Bank's support to the private sector, Finland decided late last year to seek membership in the Inter-American Investment Corporation. We see membership in the IIC as an additional opportunity to actively promote cooperation between Finland and the region and to give further impetus to sustainable development in Latin America. One Nordic country is already a member of the Corporation and three other Nordic countries are in the process of joining. To be able to put the membership to full effect, it is reasonable to expect that new member countries receive a share of influence which corresponds to their input in the IIC. I trust that we will be able to reach a solution for membership of the Nordic countries that will satisfy all parties.

The forthcoming EU-Latin America summit will provide a further opportunity to consider and give new substance to the development of the region. I am confident that also the IDB will step into the next millennium equipped with the necessary vision and resources to meet its objectives and to respond to the challenges to come. Finland has great confidence in the Inter-American Development Bank as a promotor of welfare in Latin America, and I welcome the opportunity to be your partner in our future endeavours to benefit the region.

First of all, in addressing this distinguished audience, I would like to thank the French authorities and the Bank's management for the perfect organisation of this Annual Meeting in such a unique environment of *charme* offered by Paris on the occasion of the 40th anniversary of the IDB.

Latin America and the Caribbean's economic structure and development are currently being affected by the contagion effect of the financial crisis. The turmoil in emerging economies, the dramatic drop of capital inflows (especially following the Russian financial crisis), declining commodity prices, combined with other factors and the general economic slowdown, were the main factors of the fall of the growth rate in the continent. In this difficult context we are particularly concerned with the debt problems of the countries of the region, especially those hit by natural disasters.

In addressing these problems, a new international framework for preventing crises is needed. We attach the greatest importance to the activity of the Interim Committee of the IMF, chaired by Mr. Ciampi, the Italian Treasury Minister, to improve the architecture of the international financial system and to achieve better functioning and control of the markets.

The countries of the region have rejected the temptation of inflating their economies or resorting to protectionist measures in the face of external disruptions and showed strong determination in deepening the undergoing process of structural and institutional reforms, regional integration and poverty reduction.

However, the natural disasters that have occurred in the region have disrupted the economies of the poorest countries. Italy is willing to confirm its solidarity to the victims with concrete actions. Our government responded promptly with a first contribution of US\$12 million to the Central American Emergency Trust Fund established at the World Bank to finance debt relief of the countries affected by Hurricane Mitch. A government proposal for official bilateral debt cancellation of about US\$55 million for Honduras and Guatemala is presently under consideration by the Italian Parliament. Moreover, the Italian Government will co-finance IDB rehabilitation projects in Honduras for an amount of approximately US\$21 million. We would also like to take this opportunity to stress that every effort should be made to ensure resources necessary to provide Honduras with assistance under the HIPC initiative.

We support the Bank's decision to devote particular attention, within the framework of emergency lending, to the consequences of the financial crisis on the poorest segments of the population. Coping with economic slowdown in a situation of broad inequalities throughout the region and within countries, as a recent Bank report competently and thoroughly outlines, appears to be a major challenge.

Correcting the structural imbalances of the poorest countries is another top priority of the Bank. We appreciate the efforts to improve actions in C and D countries. In this regard, we welcome the agreement on concessional resources reached last December in Washington. We acknowledge the strong effort made by the borrowing countries in making available their resources in local currencies; we urge the rapid implementation of the agreement. Italy is committed to play its own part, notably by speeding up the encashment schedule of our FSO contributions; we hope that the other non-borrowers will join us, in order to maximise benefits from the understanding reached in December.

In the midst of the dramatic developments of last year, the Bank played a crucial role in the region acting as point of reference. Under the enlightened and determined leadership of President Iglesias the Bank showed a remarkable degree of flexibility in the use of its resources, to rapidly respond to the financial crisis in the Region. The agreement reached to release emergency loans in derogation to IDB-8 replenishment regulations is a sign of a mature attitude: indeed, the Bank is not abandoning its traditional role of fostering development opportunities through poverty reduction.

A new corporate strategy is being designed by the Bank, with the aim of identifying the priorities and the comparative advantages of the institution. In our view the principle underpinning the strategic planning should be a stronger country focus, in order to address the real requirements of the borrowers and work out the necessary instruments of intervention.

An efficient corporate strategy requires a well-tailored human resources policy. Cultural diversity should be the guiding principle in the composition of IDB staff, at all levels.

Italy is ready to strengthen and diversify its co-operation with the Region. As recently confirmed by the Italian Prime Minister, Mr. D'Alema, Italy's participation to the Multilateral Investment Fund is being adopted by our Parliament. As the private sector can play a crucial role, we welcome the agreement reached on the capital increase of the IIC, as well as the entry of new members.

A "Memorandum of Understanding for Co-operation" between Italy's Institute for Foreign Trade (ICE) and the Inter-American Development Bank was just signed last Saturday, to further foster synergies between Italy and Latin America and the Caribbean.

Moreover, Italy and IDB will co-sponsor a high-level conference in Italy, in the fall of this year, on the Italian experience in developing small- and medium-size enterprises and how it could foster the development of Latin America and the Caribbean.

As an ideal follow-up to the conference, and to confirm Italy's commitment to the region and to the IDB, I am glad to announce that my government would be honoured to host an Annual Meeting of the Bank, at the earliest occasion. In this regard, we think the relevant existing resolutions of the Board of Governors should be reconsidered in order to allow nonregional countries to host the IDB Annual Meetings according to a more balanced schedule.

The present global situation requires a strong co-operative effort from the international community to address domestic and external sources of vulnerability. All the actors involved— governments, IFIs, the private sector, the civil society— should join their efforts to this aim. Strengthening partnership and confidence among IDB shareholders will be crucial to this endeavour.

ADDRESSES

FOURTH PLENARY SESSION

MARCH 16, 1999

INTER-AMERICAN INVESTMENT CORPORATION

MR. JOHN C. RAHMING, GENERAL MANAGER OF THE INTER-AMERICAN INVESTMENT CORPORATION,
TO THE FOURTEENTH ANNUAL MEETING OF THE BOARD OF GOVERNORS

I would like to thank the Government of France and the marvelous city of Paris for the warm welcome we have received on the occasion of the Annual Meeting of our Board of Governors. It is an honor and a pleasure to be here.

The Annual Meeting is a privileged opportunity to present to our member governments the progress made by the institution. It is also an excellent occasion to establish and renew contacts with financial institutions and the private sector community. Such contacts help us better define our future course of action in a concerted effort to serve the interests of all those devoted to the economic progress of Latin America and the Caribbean.

The changing and challenging environment that confronts the world's economies today confirms the need for institutions like the Inter-American Investment Corporation, created as a unique tool to support the development efforts of small and medium-scale enterprises in Latin America and Caribbean. These enterprises need the continued support and the leadership of institutions like the IIC, in order to help them to take full advantage of the opportunities arising from the globalizing economy. It must also help them weather worldwide economic ups and downs and the effects of natural disasters.

After the implementation of the 1995-1997 action plan devised to revitalize the institution, the IIC is now ready to embark on the continuation, on a larger scale, of its developmental mission. I am pleased to report to the Governors on the continued achievements of the Inter-American Investment Corporation in the pursuit of its mission.

The Year in Review

Nineteen ninety-eight was another eventful year for the Inter-American Investment Corporation. The year's target of US\$180 million in new financing transactions was surpassed by 24 percent, reaching US\$223 million. Compared to the previous year, the dollar volume of approvals increased by nearly 50 percent. Sixteen percent of the funds approved was for equity investments and 84 percent was for loans. All of the five equity investments went to developmentally-oriented country or regional investment funds. These funds have a total capitalization of US\$370 million, providing a 10:1 leverage of the IIC's own equity investments for the year. Five of the loans will be cofinanced; these operations will use US\$56 million of the Corporation's own resources to mobilize a total of US\$170 million in funding from banks and other third parties.

Noteworthy have been the Corporation's efforts to direct more resources to the smaller economies of the region. In this regard, I am pleased to report that more than 50 percent of the total amount approved in 1998 will go to the less-developed countries in the region and nineteen of the twenty-eight transactions involve financial institutions and private equity funds that enable the IIC to multiply the financing it channels to its target market. Also approved were the first mortgage securitization project, a Caribbean power debt facility and investment fund, and an innovative environmental project.

The natural disasters that affected the region, plus the ripple effects of the Asian and Russian economic crises, have greatly challenged the private sector in much of our market. The IIC's financial health has not been affected, as reflected by its level of retained earnings, but its operating results for the year were not immune to these events. As a result of these developments we decided to prudently increase provisions for potential project losses.

IIC income from all sources in 1998 amounted to US\$27.7 million. Income from lending operations totaled US\$18.2 million (US\$15.7 million from interest and US\$2.5 million from fees). Capital gains and dividend income from the equity investment portfolio amounted to US\$2.8 million. Total expenses, including US\$14.2 million in provisions, were US\$32 million, producing a net loss of US\$4.3 million. Administrative expenses for the year were US\$12.8 million, 6 percent under budget.

The IIC is working closely with the other members of the IDB Group to develop a comprehensive program for attenuating the disastrous consequences of hurricane Mitch on the people, businesses, and infrastructure of several member countries.

IIC Response to Catastrophic Events

The Corporation has taken two lines of action in response to the aftermath of this hurricane. First, we reviewed our portfolio to determine whether the repayment capacity of our client companies was affected. Fortunately, it appears that none of our projects sustained severe damage, although some banks with IIC lines of credit have subloans to companies that suffered significant damage. We are working with all of our clients to determine what actions, if any, will be necessary to restructure existing loans.

Second, we have met with government and private sector delegations from the affected countries to understand their needs and priorities for future actions. The Corporation is coordinating its response with the IDB's Regional Department, local commercial banks, and the Central American Bank for Economic Integration. IIC management has formulated a strategy that will emphasize financing projects that will create jobs, rebuild infrastructure, and provide financing to the most heavily-damaged productive sectors, such as agribusiness.

Developmental Impact

I am proud of the IIC's showing this year in terms of developmental impact. It is expected that 1998 approvals will lead to the creation of over 10,500 jobs, generate annual exports worth US\$1.1 billion, and contribute US\$1 billion per year to the regional GDP. The US\$223 million in IIC funding will support the execution of projects with a total cost of US\$1.3 billion. For every dollar earmarked by the Corporation for 1998 approvals, more than six dollars will go to investment projects.

1989-1998 Track Record

Nine full years of operations have brought cumulative approvals to 202 projects for a total of US\$986.7 million. Net commitments total US\$570 million, of which US\$489 million have been disbursed to 123 projects. One hundred and six projects have been fully disbursed. In addition, participating banks have committed and disbursed US\$290 million under the Corporation's cofinancing program.

Operations in the larger economies (A and B countries) of the region amount to US\$416 million (58 percent of the total), while operations in the smaller economies (C and D countries) total US\$224 million (31 percent of the total). Projects with regional coverage total US\$80 million. Of the IIC's committed investments, 86 percent had been fully disbursed by the end of 1998.

As of December 31, 1998, the Corporation had allocated 90 percent of its committed resources to finance small and medium-scale companies. Taking into account the projects financed directly and those reached through financial intermediaries and investment funds, the Corporation is providing support to 1,700 enterprises.

Catalytic Role

The first full nine years of operations show positive results in terms of the deployment of IIC's resources into developmental and environmentally sound projects. For every dollar invested by the Corporation, more than six additional third-party dollars will be directed towards productive investments with a total cost in excess of US\$4.5 billion. Compared to the shareholders' contribution to the Corporation's capital base, for every dollar of share capital twenty-two additional dollars are being attracted to the development of approved projects. This ratio increases to 41:1 when compared to borrowing countries' contribution to IIC's capital base. Moreover, IIC's contribution to regional economic development is evidenced by its support of projects that are generating over 102,000 direct jobs and US\$4.3 billion annually in contributions to the region's GDP.

Portfolio Composition

The Corporation now has a diversified portfolio that is managed in keeping with the strict limitations set by the Board of Directors to mitigate financial and operating risks. The portfolio comprises the following major sectors:

- Financial services, which account for one-fourth of the Corporation's active operations and enable it to provide financing to the smallest companies;
- Manufacturing, which has received 18 percent of the funding provided by the IIC;
- Agribusiness, with 15 percent;
- Private equity funds, in which 11 percent of the portfolio is invested;
- Small and medium-scale infrastructure, with 10 percent of the portfolio; and
- Mining, fisheries, and tourism, which account for 20 percent.

The IIC's loan and equity portfolio as of December 1998 reflects the strategy adopted in 1995 of increasing equity investments and financing of expansion projects. To date, 64.5 percent of equity investments have been for investments in private equity funds, while 25 percent have been direct investments in companies with expansion projects with the balance going to start-up companies. IIC loans for the expansion of existing companies represent 61 percent of the approved portfolio.

Portfolio Quality

The Corporation's loan portfolio quality is in line with its developmental mandate, with about 85 percent of outstanding investments current in payments. The remainder is either in the process of restructuring or in recovery through the execution of existing collateral. The equity portfolio is satisfactory, with realized capital gains during 1998 of US\$2.5 million. With respect to sector distribution, the Corporation followed the Board of Directors' recommended approach to reach very small enterprises through financial intermediation activities.

Reaching the Smallest Companies through Financial Intermediation

Nine full years of operations have confirmed that smaller-scale projects are most cost-efficiently reached through operations with financial intermediaries. At the end of 1998, operations in the financial sector and equity funds accounted for 40 percent of the Corporation's outstanding portfolio. Taking into account investment funds and credit lines to financial institutions, whose ultimate beneficiaries are micro, small, and medium-size enterprises, 85 percent of the IIC's funding to the region was directed to this market segment. Once the

credit lines are fully disbursed, each financial intermediary is expected to help to finance an average of twenty-five subprojects with IIC funds. The thirty-eight credit lines disbursed to date have financed nearly 700 enterprises. Funds disbursed by participant banks under IIC's cofinancing program have reached another 851 companies. I invite you to read the detailed description of the IIC's financial intermediation program included in the 1998 Annual Report.

Cofinancing Activities

The Corporation complements its own financing of companies by mobilizing additional resources on behalf of its clients. During 1998, the IIC approved transactions including US\$170 million in cofinancing funds to be raised from international banks. To date, twenty-seven international banks have committed and disbursed US\$290 million in B loans for IIC-financed projects. In many instances IIC's participation is crucial for securing the participation of other lenders, particularly in the case of projects regarded by the market as being too small to fund, especially for longer terms.

Institutional Developments

Most of the project supervision workload has now been transferred to the IIC staff located in three IDB country offices: Colombia, Costa Rica, and Uruguay. This transfer is allowing the Corporation to monitor portfolio performance more cost-efficiently and establish closer links with the region.

The Corporation has made substantial progress in achieving closer cooperation with other members of the IDB Group. IIC staff participate as members of the IDB's Private Sector Department Credit Review Committee and in the Bank's Loan Committee for all PRI projects. IIC staff also has been part of IDB Group private sector strategy missions undertaken in a number of regional countries. In 1998 the Corporation carried out 14 advisory assignments for the MIF related to its support of small and microenterprise development. Eight operations involved equity investment initiatives that are regional in scope. The others were evaluations of MIF-supported investment funds in Bolivia, Brazil, Mexico, and Venezuela.

The IIC also lent its regional expertise as adviser to the Emerging Markets Partnership for an investment fund specialized in infrastructure projects in the areas of transportation, telecommunications, energy, sanitation, and natural resources. During the year IIC provided advisory services for 35 projects located in Argentina, Bolivia, Brazil, Chile, Colombia, Dominican Republic, Mexico, Panama, Trinidad and Tobago, Uruguay, and Venezuela.

Early this year, the Corporation's Board of Executive Directors approved important policy guidelines regarding disclosure of information, inspection panels, and a revised environment and labor policy. This is part of a concerted effort to achieve greater transparency and accountability in all IIC operations. These efforts will be followed with post evaluation of projects to assess developmental impact and economic results.

Lastly, in December of last year, the Board of Executive Directors appointed me as the Corporation's General Manager. In consultation with the Chairman of the Board of Executive Directors and the Board itself, I appointed Jacques Rogozinski as Deputy General Manager. He took office in early 1999.

Program for 1999: Focus on Small and Medium-Size Enterprises

Small and medium-size enterprises in Latin America and the Caribbean have few options to obtain long-term funding for their operating, maintenance, and growth needs. Commercial banks are often reluctant to lend to companies other than large, well-capitalized firms. Foreign investors and financial institutions do not normally focus on small and medium-size companies because they perceive the potential returns to be less attractive than those in the larger-scale segment of the market. The lack of long-term funding on reasonable terms has led to severe decapitalization of the region's SMEs.

In 1999, in order to respond to the needs of small and medium-scale enterprises throughout the region, the Corporation will work on two new initiatives to complement the existing credit line program for financial intermediaries. These new programs are designed to respond to the needs of clients with smaller capital requirements, especially in the smaller economies of the region. The Small Loan Program will provide debt financing in amounts as low as US\$350,000. This program will employ the latest technology to redesign marketing, analytical, documental, and approval processes to reduce transaction costs in order to better address the needs of smaller borrowers. The use of agency lines will help reduce transaction time and cost by working in conjunction with strategic banking partners located in the region. In addition, given the underdeveloped nature of many of the region's capital markets, the Corporation will continue to support developmentally oriented private equity funds.

Meeting the Challenge

The Corporation needs to continue seeking the proper balance between profitability and developmental impact. The issue is how much credit risk the institution should take on to best meet its developmental mandate.

To meet this challenge, the Corporation has taken several steps to reduce the level of problem projects in its portfolio. These include financing fewer greenfield projects; shortening loan maturities and exiting equity investments earlier; requiring quarterly and even monthly repayments; working more with financial intermediaries; and transferring staff to the field. Also, a Special Operations Unit has been created to handle problem projects, and a Senior Credit Officer has been appointed to strengthen project risk evaluation. But more

needs to be done. The Corporation will strive to know its clients better by transferring more staff to the field; improve its project evaluation procedures; strictly adhere to pre-disbursement conditions; and introduce mechanisms for the early detection of problems and appropriate problem resolution.

Future Outlook

Ten years after the beginning of operations, the Inter-American Investment Corporation is ready to embark on an even more ambitious mission: welcome the new member countries that have applied for membership (Canada, Finland, Norway, Portugal, Sweden, United Kingdom); obtain approval of a US\$500 million increase in resources; and deploy those increased resources to reach the largest number possible of small and medium-scale enterprises. The IIC intends to do so while adhering strictly to its developmental mandate, keeping a watchful eye on the environmental impact of all the projects it finances (directly and indirectly), and maintaining tight control over its operating budget. IIC Management and staff will continue to work closely with the Governors, Executive Directors, and the other members of the IDB Group to achieve lasting progress on all of these fronts as the institution and its member countries prepare to enter a new millennium.

ADDRESSES

FIFTH PLENARY SESSION

MARCH 17, 1999

On behalf of the Government of Colombia, I would like to pay special tribute to the Inter-American Development Bank on this occasion marking its fortieth anniversary.

In his address at the inaugural session, the Minister of Finance of Colombia presented a general overview of the country's macroeconomic situation. Fiscal discipline, tax reform, exchange-rate stability, the new Peace Fund, IDB lending, felicitous borrowing on international markets, international solidarity in the aftermath of the earthquake which destroyed part of the coffee-growing region, managed inflation, and reform of the State are among our main concerns. Colombia is coming together as a nation that is determined to join in the concerted international response to the challenges of globalization.

Amid the country's fiscal problems, the national government headed by President Andreas Pastrana Arango has declared that priority will be given to ministering to the population's basic needs. Budgetary appropriations for health and education have therefore been protected. At the same time, a reform package has been introduced to make public spending on health and education more efficient and more effective.

Peace building in the area where the current discussions and the forthcoming peace negotiations are to take place and in other municipalities where the presence of the State is not felt will be based on financial support from the Peace Fund and the accumulated experience with community participation enhanced by various stakeholders in the social process under the "Colombia Plan". This plan is like a blueprint for economic and social reconstruction that will need to address specific problems such as land tenure and illegal crop substitution, as well as the traditional issues of infrastructure for development.

In a report to the UNDP, about fifty experts from Latin America indicated that education is the great equalizer or "disequalizer" in the present age. That this view dovetails with the ideas expressed in IDB documents and in the deliberations of this Board should come as no surprise. In fact, this view has been gaining worldwide currents of support since Jacques Delors presented his report entitled "Learning: the treasure within". One of the effects of this report was to spark a fruitful international discussion that was unified at least on one point: acknowledging and suggesting that education was a fundamental engine of development and equity.

In Colombia, we have launched an ambitious project for action, reform, and improvement based on the understanding that while education demands increasing public investment and has suffered from fiscal restraint, the social mobilization promoted by the Office of the President of the Republic, with the enthusiastic support of the country's social, intellectual, cultural, economic, and political leadership and rooted in modern pedagogical paradigms, offers untold opportunities for progress.

Primary education is the foundation and higher education is the guiding factor, as we have stated, to explain that according priority to primary education does not mean that we will ignore the crucial role played by higher education in a knowledge-based society. We will reach out to both international partnerships and local initiatives to consolidate the progress made in science and technology. Next week, under His Holiness Pope John Paul II, the World Federation of Scientists and the Saint Valentine Foundation will be honoring a Colombian contribution to science. The benefits of the "kangaroo" method of skin-to-skin contact for the care of premature babies, now accepted virtually worldwide, has been chosen as the "highest act of love for the human species".

Science and technology thus are viewed in our country as vital components of education from womb to tomb. The Ursulas project places the same emphasis on primary education, as the IDB has done at this Annual Meeting, based on the concept that without equity in childhood the vicious circle of poverty can never be broken. Ibuka, a Japanese writer and entrepreneur, said that "in kindergarten it is already too late" to stress the enormous fungibility in the formation of learning capacity in the early years of human life. Colombian Nobel laureate Gabriel García Márquez has touched thousand of his countrymen with his insistence on the importance of starting now to train a new generation of Colombians by erasing from the mind and the lips the traditional idea of leaving for school the task of teaching so many of the things that need to be addressed from the first few moments of life. Generating that awareness coincides with the appeal by the speakers at the seminar on early childhood which was opportunely sponsored by this annual meeting.

In this same vein, mechanisms will be offered to permit hundreds of thousands of parents to play a meaningful role in giving their children love and ensuring their readiness early in life.

The government now recognizes what over a decade of experience with community child care centers has taught. The considerable coverage achieved continues to be seen as a signal success although we have decided to modify the scheme in a move to resolve inevitable problems in terms of quality. We are moving towards establishing multihousehold centers to improve the opportunities for comprehensive child care, and particularly the supply of educational materials.

We are well aware that by simply linking early childhood policy to the development strategy, as proposed by Professor Amartya Sen, sustainable results will be achieved. Also, by making equity in child care a prerequisite for breaking the circle of poverty through tangible and vigorous actions on this front, as put forward at this annual meeting, we ingeniously help highlight the issue of early childhood and the entire social challenge.

Ms. Nancy Birdsall has put this point in its proper perspective. Problems such as domestic violence, child abuse and mistreatment, malnutrition, lack of love and education, etc. need to be taken up urgently and in terms of action since they do not allow for esoteric discussion.

In addressing these issues, their close relationship with the structural conditions of our economic and social configuration will soon be apparent in all circumstances, thus closing the loop as the connection with the entire development model becomes evident.

A UNESCO comparative study on education in Latin America, published earlier this year, found that education is highly elastic to political will, enthusiasm, and organization. There is no linear relationship between the amount of public spending in terms of GDP and the resulting quality. According to the study, Colombia was fifth in terms of education quality but scored highest in rural education performance.

We are endeavoring to protect the education budget and to increase effectiveness and efficiency. The government has decided to deepen the process of decentralization in general and decentralization of the educational system in particular. We are working to build an organizational and communicative design that strikes a suitable balance between autonomy and cohesion throughout the entire system and in each of its parts. Mobilizing the nation and reorganizing the system calls for leadership and this is more easily envisaged when there is evidence of a high public ethos for the common weal. This is the task at hand. A revolution in education is merely the forerunner to a broader movement, a cultural revolution that shakes morality to its roots, for identity in the midst of globalization, for respect for one's fellow man, for the ethics of equity, and for the conditions to live in peace.

It will cost us one percent of GDP to rebuild the coffee growing region. Over 60% of health and education infrastructure was destroyed or seriously damaged; 48,000 homes need to be built, of which 1,100 are to replace those lost by teachers in the area. Priority has been placed on mending the social fabric in order to restore the normal day-to-day routine of home, school, and work.

The entrepreneurial drive of the people in the region has begun to bear fruit. Over 100,000 children whose schools were unusable have returned to classrooms set up in camps or housed in undamaged buildings.

Colombia thanks the international community for its understanding with respect to the peace process and the havoc caused by the earthquake and reiterates its appreciation to the Inter-American Development Bank and its President, Mr. Enrique Iglesias.

I would like to thank the Government and people of France for the warm reception and hospitality extended to us. We are privileged to be your guests in this great capital city of France, a member country that also borders our country in South America, and we extend warm greetings from the people and Government of Suriname.

We wish to thank Mr. Iglesias and his staff for their inspiring and tireless support, and for their excellent and meaningful contribution towards improvement in the living conditions of the peoples in the region. We also wish to welcome Ms. Burke Dillon, our new Executive Vice President, and look forward to a continuation of the fruitful working relations we had with Ms. Nancy Birdsall.

Suriname is now prepared to participate fully in the Bank's actions to improve economic performance in Latin America and the Caribbean, with a focus on the reduction of poverty and environmental sustainability. After many years of insufficiently utilizing the excellent opportunities for development and regional integration offered by the Bank, we are now seeking support from the Bank. It is our intention to benefit more than ever from the catalytic role the Bank plays in promoting investment and growth, while this year the Bank will become a major source of external financing to Suriname. We are grateful for the support being offered by the Bank in several sectors, including trade and agricultural reform, financial and health sector reform, as well as improved macroeconomic management.

With the help of the Bank, the Japan Special Fund, and others, we intend to safeguard sustainable growth by improved environmental control. Indeed, we feel proud to mention the fact that our government has dedicated more than 10 percent of our territory as protected areas reserved for the conservation of more than 17,000 square kilometers of pristine rain forests. We are doing this in close cooperation with United States institutions and organizations, as a contribution towards ensuring the preservation of the capacity of our planet for a sustained ecological balance, which is also critical to the survival of the human species.

Like so many other countries, we are faced with a shortfall in export earnings with substantial reductions in export prices, especially for alumina, aluminum, gold, crude oil, and rice. This year aluminum smelting will be reduced by 30 percent, due to a lower than ever water level at the hydro facility in the aftermath of El Niño. This situation is further complicated by presently very low aluminum prices. In addition, we are rapidly losing preferential treatment for rice, bananas, and shrimp in European Community markets, while the traditional bilateral aid flow is substantially reduced. Despite an expected average increase of five percent in export volume, we will have eight percent less export earnings compared to last year.

In the short term we need balance-of-payments support to meet our basic import needs. Fortunately, we have a moderate level of external debt of 21 percent of GDP and debt service payments that amounted to four percent of exports in 1998. We will, however, focus our efforts to overcome the structural problem in the balance of payments, by utilizing the great potential offered by our natural resources. This we are convinced can be done effectively and efficiently through increased private investment, foremost by direct foreign investment in export sectors such as petroleum, gold and aquaculture. Our government has made private-sector-driven growth a cornerstone of our development program, and we would appreciate support from the Bank in this matter.

On January 1, 1999, we introduced a market-oriented exchange rate system. We took the bold step to unify the official exchange rate and the parallel rate, resulting in a substantial devaluation. We are seeking the Bank's support to strengthen our balance of payments through sector loans (i) for trade and agricultural reform and (ii) for financial sector reform, both combined with improved macroeconomic management and improved environmental management of our forest lands. We feel confident that a more supportive macroeconomic framework, including fiscal prudence and an appropriate foreign exchange rate policy, together with supportive sector reform measures will help us to attract private investment and grow out of the present problems.

With your help, we aspire to build our economy on a sound foundation with the policy reforms agreed upon. Those actions will increase the vitality of our economy, modernize our society, and assist us to break away from post-colonial dependency towards more efficient regional and global integration. We are fully committed to those reforms, as well as to sustainable exploitation of our natural resources, as well as towards the reduction of poverty.

Our government is fully committed to implementation of the sound macroeconomic and sector policies and programs that were proposed during this annual meeting and before, since those efforts will ensure economic growth together with environmentally sustainable exploitation of natural resources, and reduction of poverty.

We are well aware of the need for substantial reduction of our fiscal deficit. The 1999 budget is planned to eliminate the current deficit this year, and further limit borrowing for public capital investments. To this end we have increased indirect taxes on consumer goods and reduced subsidies. We will hold the line on wages for civil servants and work towards civil service reform that will reduce the number of civil servants and ensure adequacy and efficiency in the provision of public services.

The financial sector reform, which is being formulated with the cooperation of the Bank and the IMF, will be a major effort to restructure, merge, and privatize State banks. The sale of the government's share capital in two banks will complement the program, together with a major overhaul of financial legislation already prepared in cooperation with the IMF.

I would also like to mention the high expectations we have regarding the activities to foster private sector development through the combined efforts of the IDB Group, especially considering the potential of small and medium-sized enterprise development. We endorse the remarks made by so many others with regard to this matter.

Finally, I wish to emphasize the desire of Suriname to benefit from the opportunities offered by the IDB Group, as other countries that are in need of support have already experienced. The continuation of our combined efforts for sustainable improvement in the living conditions of the peoples of Latin America and the Caribbean will then undoubtedly lead to a better world for all of us, in and outside the region.

I should like to commence by conveying, on behalf of the Portuguese government and my country's delegation, our compliments to the Government of France for the excellent arrangements it has made in hosting this year's Annual Meeting. We are grateful as well for the wonderful Parisian welcome that has awaited us in this magnificent city.

The Bank's fortieth anniversary marks a milestone as we prepare to enter a new millennium. The IDB Group, through its different facilities, is deeply and actively involved in supporting all the countries of Latin America and the Caribbean. It gives me great satisfaction to underscore how much the efforts of the IDB Group in the last few years owe to the experience, vision, and leadership of President Iglesias. I will take this opportunity also to extend a warm welcome to the new Executive Vice President, Ms. Burke Dillon. And I would be remiss if I failed to mention the decisive role played in establishing the Bank in 1959 by the former President of Brazil, Juscelino Kubitschek de Oliveira, that illustrious figure and cherished friend of Portugal who has left such a mark on Latin American history.

The year 1998 was a particularly difficult one for Latin America and the Caribbean, owing to the external shocks of the financial crisis which broke out in Asia, then spread to Russia, before making itself felt in a number of countries in the region, and also because of a succession of natural disasters that have worsened the living conditions and held up the development plans of millions of people in the region. Growth fell sharply, from 5.7 percent in 1997 to 2.5 percent in 1998, and the outlook for 1999 is still highly uncertain.

Nevertheless, we have every reason to be proud of the strong commitment of the Latin American and Caribbean countries to macroeconomic stability, and of the quality of the support provided by the Bank, currently the leading multilateral lender to these countries. We have set the stage for a process of sustainable growth based on the deepening of structural reforms, as mentioned by Mr. Michel Camdessus, in an ongoing effort to narrow the public deficit but also by supporting concrete steps to spur regional integration. I would like to mention in particular Portugal's backing for President Fernando Henrique Cardoso's fiscal adjustment program, and our confidence that once financial consolidation problems are resolved and exchange-rate stability assured, Brazil will continue along an even path to sustainable development in a noninflationary environment.

The financial and macroeconomic policy instruments of the IDB Group have the capacity and flexibility to offer a quick and efficient response to the challenges posed by the process of sustainable development in a setting in which unpredictability and change are a constant. Flexibility and reforms are the key in this world of rapid technological and cultural change and globalization.

The approval of the emergency program, giving tangible form to the decision to afford the Bank greater flexibility in its resource allocation, will do much to address the goal of answering the region's needs more swiftly and efficiently.

The approval of the resolution on concessional resources, which goes to the very essence of the IDB Group's character, the spirit of solidarity amongst all of its members, will enable the institution to finance its concessional lending and technical cooperation program for the poorer member countries and participate in the HIPC initiative to provide debt relief for Nicaragua and Honduras. As for the bilateral considerations mentioned by various of our European Union colleagues concerning the level of concessionality for debt relief, as well as country eligibility, it is our view that the concepts of country eligibility, debt concessionality, and duration of programs to structure the HIPC Initiative need to be reformulated very quickly, with a view to including more countries from Latin America and shortening the debt program adjustment period. Generally, we endorse debt reduction, with the only factors of conditionality being responsible and transparent management of policies in pursuit of stable and solidary social and economic development.

We are pleased to note the impressive results posted by the Bank, particularly with respect to support for low-income and vulnerable population groups, as well as increased involvement with local beneficiaries. It is particularly gratifying to see that the Bank's activity in the social sector, including poverty-reduction operations, accounted for 46 percent of aggregate approvals.

Efforts to heighten the role of the private sector have always enjoyed Portugal's firm support. The Bank is to be commended for stepping up its activity in this sector, particularly in assisting SMEs which can be agents of poverty reduction and an engine of sustainable economic growth and social development. We likewise believe that a stronger role for private financial institutions in development financing is a condition for efficiency and equity, and is one of the unquestionable responsibilities of institutions which have interests and operations in this sphere. This is a challenge, a consequence of market liberalization that the private sector cannot avoid.

The approval of the Inter-American Investment Corporation's blueprint for the next ten years and the increase in its capital currently under discussion will enable the IDB Group to strengthen such support consistently and comprehensively.

Portugal is an active partner in all the institutions that make up the IDB Group. We intend to pursue, under the Portuguese government's program, our support for the countries of Latin America and the Caribbean, which is a firm priority on our foreign-policy agenda and for the globalization of our economy.

In this regard, Portugal was in eighth place in terms of foreign investment in Latin America in 1998 (the progression having been, in euros, 25 million in 1995, 240 million in 1996, 433 million in 1997, and 1.4 billion in 1998). These figures bespeak Portuguese investors' confidence in the future of the region overall and in Brazil and MERCOSUR in particular.

A further manifestation of these close links was the Eighth Ibero-American Summit of Heads of State and of Government held in the city of Oporto in October 1998, which forged closer political and economic ties with Latin American countries and their entrepreneurs.

Further evidence of the importance we attach to Latin America and the Caribbean are the creation of a new Portuguese Technical Cooperation Fund, of which the establishing agreement was signed on October 5, 1998, and the arrangements under way for Portugal's admission to IIC membership, so we may join in the efforts of the Corporation's present members to promote economic development in Latin America and the Caribbean, by way of increased resources for financing in the amount of US\$500 million for small and medium-sized private enterprises.

The sustainable growth of the global economy and its stable regulation depend on the collective progress of its different regions. One good example of this has been the introduction of the euro.

The IDB Group plays a key role in the advancement of Latin America and the Caribbean, a region in which Portugal is involved in solidarity with these sister nations. We reaffirm our appreciation for the efforts of all the borrowing and nonborrowing member countries, the Management of the Bank, and the staff of the IDB Group. I would also like to express my gratitude to President Iglesias for the leadership he has shown in promoting ongoing consultation between all the parties and for his capacity for dialogue and consensus-building, which are essential for successful outcomes.

To conclude, I would like to reaffirm Portugal's resolve to strengthen economic ties—through investment, financing, and trade—with Latin America and the Caribbean, which we consider so close to Portugal, and an increasingly influential and vital strategic partner of the European Union. We hope to see this borne out in fostering an international economic order in which the free market will serve society and human beings rather than continuing to make human beings and society blindly dependent on market operators. A free-market economy in the service of free individuals is our common vision.

Allow me first to express my sincere thanks to the Government of France and the city of Paris for hosting this year's annual meeting in this magnificent city.

Latin America experienced a difficult year in 1998. The region was severely affected by the global financial crisis, even though it remains committed to macroeconomic stability and structural reform. Several serious natural disasters added to the economic strain, and destroyed the lives and livelihood of thousands of people. Hence, it became a challenging year for the Bank. The situation required exceptional measures and swift action, and the IDB demonstrated its ability to respond rapidly to the needs of the region in extremely difficult circumstances.

Norway was pleased to see the IDB, together with the IMF and the World Bank, play a constructive part in the coordinated effort to help prevent the crisis from spreading throughout the region. The crisis is not yet over, and it is likely to continue well into 1999—perhaps beyond.

What should be the role of the IDB in the ongoing efforts to resolve the crisis? The IDB's strength is not financial crisis management or balance-of-payment support on a large scale. This is primarily the role of the IMF. In our view, the IDB should be guided by the following when it takes part in financial emergency lending operations: (1) The IDB's involvement should be of a temporary nature, and should not alter the Bank's main objectives to alleviate poverty and to promote long-term development. (2) The lending should not weaken the Bank's financial position. (3) It should be based on close coordination with the IMF and the World Bank. (4) It should not be used for regular balance-of-payment support, but to address the structural causes and social consequences of the crisis. (5) Last, but not least, emergency lending programs should not be done at the expense of the long-term needs of the poorer countries in the region.

Last year's natural disasters caused extensive and long-lasting damage to some of the poorest countries in the region. "El Niño", "Hurricane Georges" and "Hurricane Mitch" left the affected countries devastated. The IDB is to be commended for its quick response to these natural disasters, especially after "Hurricane Mitch", through which the Bank confirmed its leadership role in the region.

Norway contributed about US\$25 million in emergency assistance to Central America last year. Norway was also an initiator of the trust fund to assist Central American countries with multilateral debt service, which was established together with the World Bank, and Norway was the first country to provide a substantial contribution, of nearly US\$16 million, to the fund.

Natural disasters are unfortunately likely to happen again. In this respect it is important for countries that are prone to natural disasters to focus on preventive measures and disaster preparedness. The Bank's newly approved policy for "emergencies arising from natural and unexpected disasters" should help the Bank and its regional members to address this problem. However, I would like to emphasize two concerns. Firstly, we need to further strengthen the coordination and cooperation between all actors—including the IFIs, the UN organizations, and the NGOs—in humanitarian operations. Secondly, we need to adopt a more integrated and comprehensive approach to short-term relief operations and long-term development. The response after Hurricane Mitch might well be a model for the future.

We look forward to the CG meeting in Stockholm, and we are prepared to respond to the affected governments' plans for reconstruction and transformation, that we understand are under preparation.

The reconstruction needs of the affected countries in Central America will be considerable, and concessional resources will be needed. Therefore, we appreciate the agreement reached last December on the replenishment of the IDB's concessional resources. We regard this agreement as a demonstration of regional solidarity among Latin American countries, which we very much welcome.

Debt relief has become a central part of the emergency program in Central America. This demonstrates the growing recognition of the importance of including debt relief in a comprehensive development approach. It is both a moral obligation and an economic necessity to address the unsustainable debt burdens of the poorest countries. The HIPC Initiative provides us with a historic opportunity to act. We should use the on-going review of the HIPC to identify ways of improving the initiative in order to provide faster and deeper debt relief. We look forward to progress in this direction at the coming G7 Summit. Recognizing the importance of concrete action, Norway recently approved a national debt relief strategy, one element of which is additional bilateral debt relief on top of exit solutions under the HIPC mechanism. We encourage other bilateral donors to make additional efforts to enhance the effect of the HIPC Initiative.

Let me now turn to some Bank policy matters. We welcome the increased lending to social sectors, which is well above the target of 40 percent set by the Governors. However, lending to C and D countries was still below the indicative target of 35 percent in 1998. We trust that the ongoing action plan for C and D countries will continue to improve the Bank's services to the poorest countries.

With regard to the Bank's ability to address cross-cutting issues, we continue to be concerned about the limited staff resources of the WID Unit and the newly established Poverty Unit. Mainstreaming gender issues within the Bank and in the region continues to be a challenge. Norway has supported the WID Unit and several gender projects for many years, but the latest report on the WID action plan shows us that we still have a long way to go. We are looking for a renewed commitment from the Bank, but also from its regional member countries.

We continue to be impressed by the Bank's innovative work in the area of modernization of the State, which has made it one of the leading international institutions in support of public-sector reforms. Less emphasis has been placed on civil society. The changing role of the State, increased emphasis on local government, and other factors, underline the need to further define and develop the Bank's partnership with civil society. We therefore urge the Bank to develop its own strategy for the strengthening of civil society. We welcome steps in this direction through the initiatives to promote social equity in the region—in partnership with governments and civil society. Raising awareness of the ethical dimension of development is another interesting proposal.

At its Fortieth Annual Meeting, the IDB is recognized as a full-fledged development institution. Over the last decade the Bank has undergone profound changes and has become the single largest multilateral lender to the region. But we must not cease to change. The Bank needs to continuously adapt to the needs of its borrowers.

One of the main challenges for all of us is that of information technology. Information technology is erasing boundaries and distance between countries, societies, and individuals all over the world. New economic opportunities are emerging for rich and poor alike, and old ways of doing business—both in the public and private sector—are becoming obsolete. We must all adapt. And so must the IDB, in order to stay relevant and help its clients to adapt.

I would like to reiterate our request from last year, that a more visionary document on the future direction of the Bank be presented for discussion among members. This document should take us beyond the more internal corporate strategy work presently taking place within the Bank. As we embark on a new millennium, the Bank needs to assume its leadership role in the region by defining its own role in an increasingly global and complex environment. Coordination and partnership with other institutions, as well as with civil society, will be of vital importance in the future. This requires a clearer understanding of the IDB's comparative advantages and priorities, and an assessment of their implications for the Bank itself. The address delivered by President Iglesias last Sunday is an interesting first step in response to this challenge. I would encourage the Bank to build on the President's reflections, and to take the discussion further.

In conclusion, I would like to confirm our general satisfaction with the work being carried out by the Bank and its staff. I look forward to a further increase in the cooperation between the IDB and Norway, including by becoming a member of the IIC, and I can assure you that Norway will continue to support the Bank's work.

The Paraguayan delegation is pleased to have this opportunity to attend the Fortieth Annual Meeting of the Board of Governors, the last meeting to be held in this century and the first for the administration of President Raúl Cubas Grau, which we are representing in this beautiful and historical capital of France.

We would like to commend the local authorities for the superb organization of this event, and also to express our sincere thanks for the warm and friendly reception that we have been accorded.

In the last few years, Paraguay has made significant progress towards consolidating the democracy to which our people have aspired for so long. Last August 15, the third democratically elected administration took office in what were the country's fairest, most by-the-rules elections since the difficult period of political transition began. It is now fostering honest, frank, and responsible political dialogue among all the country's political leaders and sectors. In this same vein, an anticorruption campaign will be launched in the coming days by the government with the participation of civil society, the Church, the legislative and judicial branches, and international organizations, with a view to promoting comprehensive institutional reform programs to combat corruption, contraband, and the drug trade.

Our country has not been immune to the effects of the international economic crisis, and was also adversely affected in 1998 by extreme weather conditions, financial system imbalances, and mainly by the slowdown in growth in countries in the region, particularly our principal trading partners.

Notwithstanding these difficult economic conditions, which take their toll on social programs, our government has given top priority to the process of structural reform, which had become bogged down in recent years. In addition to short-term initiatives to spark economic recovery and stabilization, job creation, industrial restructuring, and financial system reform, a cornerstone of our government's agenda is structural reform that includes a legislative package now before Congress to rehabilitate the financial system, ensure sound investment of social security funds, the privatization of one half of the State-owned telephone company and of 80 percent of the State cement company, and the creation of regulatory agencies for the electricity, water supply, and sanitation sectors, which will make for heavy investment in basic infrastructure over the next few years. Ports and airports would be operated by the private sector as concessions.

By the end of its first year in office, the administration will have submitted to Congress a bill for reform of State-owned banks, a bill to create an environmental regulatory agency, a bill to reform the Ministry of Agriculture, and laws governing State financial administration and government procurement.

In the area of economic recovery, a supply of local counterpart funding is assured for investment projects using external credits, as well as increased coverage by the Guarantee Fund for microenterprise and small and medium-sized businesses; also, more resources are being allocated to the Industrial Development Fund. These measures are intended to boost investment and generate employment in the local market.

One of the main tenets of the present administration's economic policy is consolidation of fiscal equilibrium. Since taking office, the government has adopted administrative measures to streamline the use of State resources, to control public spending. Major efforts have been made to improve tax collection and to reverse the decline in recent years through program-sharing with the private sector in procedures to raise the efficiency of tax administration. By reducing tax evasion, we will be offering economic agents greater equity and fairer access to economic opportunities.

Thanks to the actions undertaken by our administration, at the close of the 1998 fiscal year a deficit equivalent to 0.9 percent of GDP was posted, less than the 3 percent initially projected. As a result of this success, year-to-year inflation declined from 14.6 percent in December to 11.5 percent this February. Thus, there is every reason to believe that the 1999 inflation target of 12 percent will be met.

In the area of decentralization, we are just commencing a process to promote greater participation by local and departmental governments in the design and implementation of public policies. Successful completion of the current Pilot Plan will bring all subnational administrations into the national budgetary process for fiscal year 2000.

On the social front, the national government has given priority to investment in human and social capital as the sole alternative for laying the foundations for sustainable and equitable development in the country. To this end, we are making every effort to consolidate educational reform by decentralizing spending on education, training teachers, improving school infrastructure, and establishing mechanisms to monitor the quality of education.

We are also working to improve health conditions and nutrition for Paraguayans by extending primary health care coverage to the entire nation and providing free obstetric and child care, as well as through national programs to reduce mother and child mortality and institute epidemiological surveillance, and efforts to control parasitic, nutritional, infectious, and noncommunicable diseases and chronic illnesses, the latter being, as in many other countries, fairly prevalent amongst adults.

We have been developing programs to provide support to children, an area that our government considers one of the best investments for combating poverty now and in the future, and, accordingly, for creating a more equitable society for all. The Secretariat for Social Action has been promoting an IDB-financed program to address the problem of street children.

The successful Microenterprise I and II programs, with which our country has been moving forward with impressive results, reaffirm our unflagging support for an area of our economy that may soon become the engine of growth for our development, considering that SMEs account for a large share of the nation's economy. We would therefore like to commend the member countries of the Inter-American Investment Corporation for their formidable efforts in setting the stage for increasing the Corporation's capital.

We fully endorse the priorities established by the IDB in the allocation of its resources, since we consider poverty reduction and social investment to be essential for sustainable economic and social development in the region. Other areas, such as modernization of the State in all of its aspects and integration into the global economy, serve as a basis for attaining desired levels of investment and growth. Also, we value highly the support shown by the Bank for investment in infrastructure and assistance for the private sector in a context of environmental planning and conservation.

Lastly, I would like to convey the Paraguayan government's commendation for the work of the authorities of the Bank and the Corporation, and in particular the leadership of President Enrique Iglesias, without whose efforts the initiatives of the borrowing countries might not have materialized for the benefit of their people. Accordingly, I urge the other delegations to support the strengthening of both institutions so they may continue to further the development of our countries. We also welcome Ms. Burke Dillon, the Bank's new Executive Vice President. We are confident that she will make a valuable contribution to the attainment of the institution's objectives, and we wish her every success.

I would like to begin by extending our greetings to the Inter-American Development Bank—represented here by its president, Mr. Enrique Iglesias—on the occasion of the Fortieth Annual Meeting of its Board of Governors and Fourteenth Annual Meeting of the Board of Governors of the Inter-American Investment Corporation. Over the past 40 years, the IDB has been both a steady ally and an important partner in our region's development process.

In this connection, we welcome the creation of new forms of support, such as the emergency lending programs and the capital increase of the IIC.

Peru is also grateful for the Bank's contribution to the national peace process and the economic modernization and social development efforts undertaken by the administration of President Alberto Fujimori throughout the 1990s.

Thanks to the hard work of Peru's citizens, the support of the international financial community, and the confidence of investors, Peru today is a very different country than the one depicted in the 1980s.

Violence has given way to peace, insecurity to stability, despair to confidence in the future, and isolation to integration in the world economy.

We have a very clear idea of our goal: we want to be a developed country that is open to the world, with economic growth, employment, and quality education for all Peruvians.

This vision, which is shared by the national government, business sector, and civil society, is what spurs us on in the shift towards becoming a strong market economy that is both competitive and open to the world.

Although the adjustments implemented since the beginning of this decade have been difficult, we refuse to fall back on protectionist policies, which are now a thing of the past.

In this connection, I would like to reaffirm that Peru is a country that looks towards the future rather than the past. Its sights are set on a twenty-first century full of optimism and confidence, and it will not veer from its policy whose economic underpinnings are the market and private initiative and whose political foundations are democratic principles.

Between 1993 and 1998, Peru grew at an average annual rate of 6.2%. Currently, inflation stands at 6% per annum, international reserves are equivalent to 14 months of imports, and foreign investment continues to flow into the country, despite the impact of external shocks.

Our target for this year is GDP growth of between 3% and 4.5%.

According to IMF estimates, Peru will be the Latin American nation with the strongest growth in 1999, in contrast to the regional trend toward a slowdown.

Without a doubt, 1998 was a dramatic year, both for our country and for the region as a whole. The El Niño phenomenon, the Asian crisis, and the turmoil in Russia affected production and employment, and dampened the prospects for growth.

Even so, we have weathered the crisis with solid macroeconomic instruments, which were the result of our sound economic policy and the enormous efforts made by the country during this decade.

We are currently enjoying an economic upswing, and the policy we are pursuing provides a guarantee of a solid financial system and an economically viable business sector.

Negotiation of the third extended facility with the IMF is a clear sign of Peru's commitment to macroeconomic stability.

The government's program for 1999-2000 has three core objectives: stable growth, reduced unemployment and underemployment, and lower levels of extreme poverty. All sectors of government have assigned priority to meeting these objectives.

Against this backdrop, Peru's economic program seeks not only to solve those of its current problems that were triggered by the external crisis, but also to consolidate second-generation reforms aimed at strengthening institutions that ensure the sound operation of the market, as well as good governance and efficient, transparent public administration.

Peru's situation has been strengthened by the signing of the peace agreement with Ecuador last October. This is a landmark event for regional stability, and it represents a solution to a historical conflict that existed between our nations since the 1800s, limiting their possibilities for integration and development.

Today, as Ecuador is grappling with a difficult social, economic, and financial situation, we would like to express our support and solidarity on behalf of the government and people of Peru, and our hope that the current crisis will be solved quickly and that Ecuador will emerge with a strong economy and strong democratic institutions.

Peru's admission to the Asia Pacific Economic Cooperation Forum (APEC) last November was yet another milestone in the process of integration into the global economy.

Our membership in APEC represents an additional advantage that Peru can offer to investors, in its capacity as a privileged "bridge" for integration between South America and the Pacific Rim.

I should like to stress that the Peruvian government is firmly committed to the eradication of extreme poverty. We have set ourselves a target of reducing this poverty to a level of 10% by the year 2000.

To achieve this, we are pursuing a public-investment strategy that is targeted at more efficient social spending, to ensure that funds are truly channeled to the neediest groups.

We are well aware that a country with inequalities and excluded groups cannot survive for long. Investing in people, health, and education is the best guarantee for gradually closing social gaps.

A cornerstone for Peru's development efforts in the twenty-first century will be quality education.

I bring you, then, a clear message from my country. We have accomplished many important achievements this decade: economic stability, peace at home and with our neighbors, and integration into the global economy.

The challenges now facing us are just as great: growth with equity, development of the market and democracy, stronger institutions, and broader opportunities for all.

These challenges, however, do not intimidate us. On the contrary, we are rising to them with the same resolve and conviction that have characterized Peru's actions and work since the beginning of the decade.

The dawning of a new millennium is a propitious time for renewing our faith in a nobler destiny for all men and women on the planet.

The twenty-first century will find Peruvians working, creating, and contributing, day by day, towards the construction of a more humane and just world.

ADDRESSES

SIXTH PLENARY SESSION

MARCH 17, 1999

CLOSING SESSION

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,
AT THE CLOSING SESSION

Honored Ministers and Governors:

In concluding the activities of this Fortieth Annual Meeting of the Board of Governors of the Bank and Fourteenth Meeting of the Inter-American Investment Corporation, I want to thank you and your colleagues for your support in making this event a success. Special thanks are due to President Chirac of France for his kind invitation to host this meeting in Paris, as well as to the Prime Minister and all the members of the French government who have joined us here.

Those of us who attend these meetings every year know the tremendous amount of work their organization entails, and on this occasion it was performed with dedication and a great spirit of friendship for the Bank and for Latin America and the Caribbean. We appreciate these efforts very much.

I also want to thank the French private sector for its important contribution, and the individuals who participated in the various seminars for making the discussions so interesting.

I would now like to touch on a number of issues that received particular attention over the past few days. The reflections on the Bank's first 40 years were particularly memorable, not as a form of nostalgia for the past, but rather as a basis for looking to the future. I wish to thank all who participated for their expressions in support of the institution, its President, and all of my colleagues. Your words can only strengthen our commitment to serving the region.

In recent years, the annual meetings of the Board of Governors have included seminars and meetings organized by the Bank's Management in cooperation with host governments and the private sector. This year, we held 12 such meetings, all of which provided useful lessons and valuable insights, enabling both participants and the Bank to take the pulse of the most varied segments of our societies.

The first of these events, held at UNESCO headquarters, was attended by some 100 young people—under the age of 40—who reflected on the challenges to be faced by Latin America and the Caribbean in the next millennium. Their discussions were fresh, constructive, and intelligent and, in seeing how this new generation perceives the problems ahead, left us with a feeling of optimism. These young people displayed idealism but also a good dose of pragmatism. They recognize current realities and the tremendous challenges to come, and thus can avoid the excesses that sometimes accompany youth.

Another seminar was devoted to culture and development. The important role played by culture in the development process was a subject we particularly wanted to examine here in France, a country that has given much to universal culture and to our own particular heritage. To gain a comprehensive vision of development, we believed it was important for individuals from the world of culture to share their perspective on the meaning of development. During this seminar, new approaches to education and socialization were analyzed as responses to cultural change and to the desire for greater participation in civil society—with public policies forming a bridge between government and community values. Particular attention was drawn to the importance of social capital and public participation in economic and social development and the building of democratic societies. There was a clear conviction that society must not be reduced to its purely economic aspects, that we must look beyond the realm of economics and social science and draw on our cultural roots and values. The constructive discussions that followed highlighted culture as an industry and source of employment throughout the world and in Latin America and the Caribbean in particular.

With respect to social issues, there were two seminars I would like to mention. One concerned the issue of inequality. This was the subject of our most recent Economic and Social Progress Report, examining why our region is the most unequal in the world. Our discussions here in Paris were extremely useful. The other seminar concerned the importance of early childhood intervention in breaking the vicious circle of poverty. As explained in that seminar, investing in children to avoid passing on poverty from generation to generation is the best investment our region can make. Studies by the Bank and other institutions have shown that investing in early childhood—attacking poverty at its roots—yields benefits for children and their communities while reducing subsequent social costs. Both seminars played an important part in this year's meeting, underscoring social issues once again as a central focus of Bank activity.

One subject that necessarily commanded our attention this year was the issue of economic turbulence: the problems of financial volatility and the risks and opportunities associated with globalization. The seminar on "New Initiatives to Tackle International Turmoil" provided for intense discussion and debate, from a wide variety of perspectives, on the problems being encountered with financial and monetary architecture—national as well as international. It should be remembered in this context that it is not the Bank's function, as an institution, to offer prescriptions for such problems, but we do seek to promote discussion. In this case there was considerable controversy because each country has its own way of analyzing financial architecture, but conclusions were reached nonetheless. It is important for such discussions to continue and, above all, for financial coordination mechanisms in Latin America to be strengthened. The seminar on "The Euro and Its International Impact" addressed similar issues, and a wealth of ideas were put forward. In my opinion, it has contributed tremendously to current thinking on Latin American integration. In our determination to integrate, we must also begin to consider how to make monetary policy the culmination of our integration process, as it has been here in Europe.

A variety of private sector issues also received attention. The seminar on "Private Sector Participation in the Development of Latin America" emphasized how financing from multilateral institutions and the establishment of associations between European and Latin American businesses are key factors in helping small- and medium-sized enterprises to compete in a global economy. It was

explained how joint ventures can result not only in transfers of capital, managerial knowledge, and production techniques, but also in various forms of business cooperation, meeting needs for growth and market power, and seeking out synergies and complementarities. The importance of technology and the bridge for its transfer between Europe and Latin America were identified as an area for continued work in the future.

Our discussions covered various specific topics of current concern to the region in which European experience has also been instructive. One seminar, for instance, addressed the issue of decentralization, which has long been a subject of mutual interest. In that area, we have much to learn from Europe. On the subject of pension funds, discussed in another seminar, we may have contributions to make to Europe, given our experience and innovations in this field in Chile and elsewhere.

These, in broad strokes, were some of the contributions made at the working sessions held during this Annual Meeting—in addition to presentations by several Governors on national issues. The Brazilian authorities, for instance, outlined their economic program.

I would like to turn now to the central messages conveyed during our Annual Meeting and the conclusions that can be drawn about Latin America and the Caribbean at the end of this century. First, our region has clearly stayed the course on the processes of reform, openness, and institutional renewal, with a view toward modernization and active partnership in the international community. It is now a region of some 500 million inhabitants, with a combined output of more than US\$17 billion.

Second, although the region faces problems, it has demonstrated an ability to react rapidly. Drawing perhaps on lessons from past experience, the region responded swiftly to counter the effects of international turbulence. Prior experience was also helpful in controlling expectations, which is critical to avoiding further crises. The region's response took the form of monetary and fiscal adjustments as well as currency devaluations for certain countries, reflecting a desire to avoid the inflation of years past. The distorting effects of inflation and a respect for balanced macroeconomic adjustment appear to have been engraved in the collective memory of our people and their governments.

Along with confidence in the region's reactive capacity, there was also a sense of consternation at the prospects for 1999. I am confident that, with continued reform, the year 2000 can mark the beginnings of renewed growth. The region can, in particular, be expected to benefit from economic growth in the United States, Europe, and Japan.

Certain items of unfinished business were also discussed. It was noted that the process of reform in Latin America and the Caribbean is still incomplete, particularly as regards labor reform and greater flexibility in labor markets. The importance of financial system reform, especially social reforms, was also emphasized. The Governors addressed the subject of governance both in the broad sense and in terms of government institutions. The need for progress in the areas of transparency and corruption and the role of the private sector in the new economic context were further subjects of discussion.

But perhaps the most profound message conveyed during this meeting was the sense that, although the region has shown a vocation for integration for decades, we must now redouble our efforts in that direction. An integrated region will clearly be better positioned to navigate the world's increasingly global economy.

I want to take this opportunity to thank the Managing Director of the International Monetary Fund for his presence and for sharing his valuable insights on the new international financial architecture. I believe Latin America and the Caribbean will gain particular benefit from participating actively in these discussions at all levels, so as to have a voice in the new regional financial architecture.

As far as the Bank is concerned, I would describe 1998 first as a year of emergencies—in economic and financial terms and in the wake of natural disasters—and second as a time for restructuring the institution's concessional resources.

With respect to the financial emergency, we provided the countries with US\$9 billion. Here I again want to stress to the Governors that such resources are available for all member countries, not only the more developed economies. Small countries are in fact drawing on this fund as well. Another point worth stressing is that our efforts in this area are coordinated with those of the International Monetary Fund. The emergency financing we provide supports financial reform and recovery, but, more importantly, it is accompanied by resources to address social problems. We are not the International Monetary Fund, nor do we wish to be; our function is to support economic and social development. However, we can provide assistance in emergency situations by helping to mitigate the social impact of crises, which is part of our job.

With respect to natural emergencies, the task has been considerable. We wish to thank all of the governments for their assistance and invite them to continue supporting our efforts, particularly at the meeting to be held in Stockholm in May of this year. That meeting will explore ways to assist Central America in coping with the damage and related difficulties caused by Hurricane Mitch. The goodwill you have expressed has been an inspiration to us.

We are also pleased that an agreement was reached on concessional resources. This was not an easy task. The negotiations were difficult from the start, but the final agreement reflects a strong spirit of solidarity among our countries. This was the first time that countries in the region, through collective sacrifice, have resolved to support the countries eligible for concessional resources, supporting debt reduction, although it is true that the burden fell mainly on the Bank's borrowing countries.

I must say again how gratified I was by the willingness of several nonborrowing countries to accelerate their contributions, as requested by a resolution of the Committee of the Board of Governors. I would like formally to invite the borrowing countries to consider this gesture as a form of assistance in the process we have undertaken.

Finally, we come to the matter of the Bank's vision. I should point out that our work in this area has been a joint effort by the Board and Management, and I consider it very fruitful. The four working groups on evaluation, procedures, human resources, and, in particular, the Bank's corporate strategy have played a fundamental role and have my full support and commitment—on a personal as well as an institutional level. I should add that a proposal has been made by the Government of France and supported by several Governors to hold a special meeting of the Committee of the Board of Governors each year to discuss the economic situation of Latin America and the Caribbean and its implications for our internal policies. This will be a subject for discussion with the Board, which will in turn convey the results to our Governors.

Given its origins, the Bank has a number of natural advantages: it is an eminently Latin American and Caribbean institution that has distinguished itself since its foundation by a focus on social concerns and, above all, a dedication to serving the member countries as effectively as possible. Knowing the Bank to be a friend and partner in economic and social development, several of you have advocated that we maintain an ongoing dynamic and forward-looking vision in tune with the times in which we are living. That will not be easy.

We are now taking on a second generation of reforms, involving sensitive areas of society, values, and traditions. This second generation of reforms will be much more complex than the first. We will be entering new terrain. It is far more difficult to develop programs for education, health, and pensions, for instance, than to change a system of tariffs.

Fortunately, we can count on a spirit of solidarity among our countries. The Bank has the privilege of working for a region with a profound sense of solidarity. The cooperation shown during the recent natural disasters and in the area of concessional resources has made this clearer than ever. But we can also count on cooperation from the nonborrowing members—the United States, Canada, Europe, Israel, and Japan are all partners in the same enterprise. Meeting in Europe gives us the opportunity to express our thanks to the nonregional countries for their continuing support and their responsible and active participation on the Board. We can be confident that the Rio de Janeiro meeting, to be held in June, will serve to further strengthen ties between the old continent and the civilizations of Latin America and the Caribbean—a diverse region, combining strengths and energies from many sources, where Europe has had a particularly far-reaching influence.

Honored Governors: I thank you again for your cooperation and for the great honor of having you present for this historic meeting.

Here we are at the end of what has been a highly productive meeting with fruitful exchanges of views. I think that the number and quality of the participants attest to this success. Six or seven thousand people, including specialists, senior government officials, and businessmen from a total of 46 countries, assembled here in Paris for this annual meeting of the Board of Governors of the Inter-American Development Bank, sending a clear message of the international community's interest in the institution.

Also indicative of this success is the quality of the ideas developed over the past few days, particularly during the various seminars in which some of the finest experts took part. I was struck by the quality of the discussion on the financial crisis and, at the seminar I participated in yesterday, on the euro, as referred to just now by President Iglesias. It seems to me that in both cases, with a financial crisis involved and just weeks away from the meetings of the Bretton Woods institutions in Washington, the light shed on this subject here is useful and provides a better understanding of the need to reform and transform the international monetary and financial system. The comments made by the various participants have done much to enrich the discussions we will be having in Washington in just over a month's time.

As to the euro, the issue of European monetary and financial integration was clarified, at a time when Latin America is questioning its ability to move forward with regional integration. What we can do is stand by you. These operations are complex and take time, but the European experience may perhaps be helpful to those of you who are tempted to press ahead with the process of regional integration, either within Mercosur or through some other arrangement in Latin America. There were also many useful exchanges on the issues that have traditionally been associated with development, energy, insurance, and the fight against inequality and poverty.

These discussions were all highly successful for Latin America and for the issues of development and finance with which we are concerned. Each country's contribution was considerable and I would like to thank you all. It was also a great success for the Bank itself. I believe that there is a consensus among the Governors that they have confidence in the Inter-American Development Bank and are satisfied with its operations. I believe that this consensus is broad-based and I am very grateful to President Iglesias for his personal commitment to the Bank's efforts and the momentum he has given to the issues. I think I speak for everyone, President Iglesias, in saying that you have the support and recognition of the Governors. As you are aware, France is committed to strengthening good governance at our international institutions, a feeling that is shared, I know, by President Iglesias. Many of the Governors have expressed support for the French proposal that the Committee of the Board of Governors hold a meeting of ministers once a year. I would like to thank you for this support and would propose, with President Iglesias's agreement, that the Development Committee for Latin America meet this autumn in conjunction with the meetings of the Bretton Woods institutions.

The Bank's fortieth anniversary is also a time for renewal. This annual meeting marks an important turning point. It has confirmed a series of far-reaching and forward-looking decisions which had been in the works for some time but which only now have come to fruition. I am referring, of course, as Mr. Iglesias noted a few moments ago, to the concessional resources which are assured for a long time to come, reflecting a strong show of solidarity on the part of the countries in Latin America since the more developed ones in the region contributed significantly to this effort. I am also referring to the capacity that the Bank now has to intervene early at times of crisis such as in the recent case of Argentina. I think, further, that the increased resources the Bank Group has now been given to pursue its activities, the US\$500 million increase in the capital of the Inter-American Investment Corporation, is important as well. I believe that we may congratulate ourselves on the fact that this process has been completed. Obviously, much remains to be done to implement these initiatives and as you are aware a meeting of the Committee of the Board of Governors is to be held in Paris in May to finalize all of these decisions.

Before concluding, I would like to say a few words about the Governors' endorsement of the effort under way to fulfill one aspect of the Bank's mandate: namely, to provide financing for long-term development. This ties in with the focus you have given to development and culture at this meeting. Let me recall the importance of culture for the development of individuals, society, and institutions. I know that President Iglesias has a particular affinity for and attaches great importance to cultural affairs, as we have seen at UNESCO in the past few days.

Lastly, I hope that in addition to these highly satisfactory and encouraging results, all of you have been able to enjoy your stay in Paris. The government has made every effort to arrange for fine weather and the Bank has arranged for a number of events to be held in conjunction with our annual meeting, which in my judgment have been of the highest quality. I hope you will find a little of this French touch again next year in New Orleans; so, let's make a date to meet on Bourbon Street in a year's time. On that pleasant note, I hereby adjourn this Fortieth Annual Meeting of the Inter-American Development Bank and Fourteenth Annual Meeting of the Inter-American Investment Corporation.

ADDRESSES

OTHER

MARCH 17, 1999

Allow me to start my address by expressing sincere congratulations to the management and staff of the Inter-American Development Bank for successfully fostering the development of the countries of Latin America and the Caribbean for the last 40 years. As an important provider of finance and expertise for the region, the Bank has successfully met its basic targets throughout this time. Delivering an innovative and diversified lending program in synergy with tailor-made projects, it managed to remain the region's main source of multilateral finance for the last five years, thus bolstering its members in their efforts to alleviate poverty and social inequality, build infrastructure, support the private sector and reform institutions. In this connection I should like to commend President Iglesias for the results the Bank has achieved under his leadership. It is my firm belief that much of the credit for turning the Bank into a flexible and "borrower-friendly" institution and for its enhanced credibility should go to him.

Nineteen ninety-eight was a difficult and challenging year for the world economy and the region. Repercussions of the Russian crisis on the financial sector were exacerbated by natural disasters caused by El Niño, hurricanes Georges and Mitch, and finally by the earthquake in Colombia. Destroying human lives, physical infrastructure and disrupting production, they compounded difficulties for many countries of the region. Although growth slipped to about 2.5% compared to over 5% in 1997, only two countries experienced negative rates. Thanks to the Bank's early response and a firm commitment of the region to macroeconomic stability, inflation remained under control and fundamentals for future growth remained in place. Remaining committed to free market policies we believe that countries of Latin America and Caribbean should keep their important position in attracting foreign direct investment and equity once the capital flows have recovered.

We note with satisfaction that the Bank responded rapidly and effectively to the sudden reversal of capital flows to the region and to the catastrophic natural disasters through appropriate instruments and an adequate volume of lending, demonstrating both its flexibility and its catalytic role. In this connection we would like to express our belief that the instrument of the special emergency lending program justified its existence. However, we would like to request the management to take all necessary precautions to avoid the temptation of loosening conditions for granting such loans. It should not be forgotten that the instrument of policy-based lending, with fast-disbursing components as a regular tool to address similar issues, is still in place in the Bank.

Therefore, we urge the Bank to remain committed to the reduction of poverty and social inequality, as the priority areas of its Eighth Replenishment mandate. We are pleased to learn that the amount of resources committed to social sector programs increased to 46% of total lending in 1998. In this connection we support the Bank's focus on the availability of appropriately designed and delivered services and projects that directly benefit the most vulnerable segments of the population in the countries of the region. We welcome sector strategies and operational policies such as the Rural Poverty Reduction Strategy approved last year. At the same time we are aware that poverty alleviation cannot be successful unless it is supplemented by properly elaborated programs of education, health care, social security reform, labor market development, etc. Pursuing the priority targets we would like to encourage the Bank to continue complementing its lending instruments with non-lending activities such as research, training, advisory services, consensus building and others.

Looking at the IDB's priorities and supporting its flexibility we have no doubt that the Inter-American Development Bank is and should remain primarily a development institution, capable of properly responding to the diverse needs of its borrowing countries, especially to those of its poorer and smaller members. In this respect we are pleased that the agreement on concessional resources of the Bank and related matters has been finally reached. We find it important that the funding requirements of the FSO for the next ten years will be fully met from within the Fund itself. Bearing in mind the fact that the said agreement is a compromise, we request the management of the Bank to make every effort to enable its implementation. We trust that the long-standing history of regional solidarity and support for the smaller member countries shall be reaffirmed by a proper response of the members. In this connection it is my pleasure to inform you that the Government of the Republic of Slovenia is willing to consider the possibility of accelerating encashments of its FSO commitments under Eighth Replenishment as soon as 1999.

To maintain its relevance as the crucial development institution of the region, the Bank should remain focused on the priority areas. Yet it is the changing world and the uncertainties it is bringing along that dictate the need for the IDB to flexibly respond to the new challenges with innovative approaches and instruments as well as by improving its efficiency. The ongoing process of preparation and updating of different strategies and policies of the Bank represents an important step towards this target. We are convinced that the Bank will find comprehensive and feasible solutions, to the mutual satisfaction of all the member countries, which we are supporting and awaiting with great interest.

I should like to conclude my address by expressing sincere appreciation on behalf of the Government of the Republic of Slovenia, to the Government of France and to our host, the charming city of Paris. We thank the IDB management and staff for their excellent preparation of this Annual Meeting and for the hospitality extended to us on this occasion.

¹ Distributed for information during the 40th Annual Meeting of the Board of Governors of the Inter-American Development Bank.

**REPORT OF THE COMMITTEE OF THE IDB BOARD OF GOVERNORS
ON ITS ACTIVITIES SINCE THE LAST ANNUAL MEETING**

**REPORT OF THE COMMITTEE OF THE IDB BOARD OF GOVERNORS
ON ITS ACTIVITIES SINCE THE LAST ANNUAL MEETING**

The Committee of the Board of Governors, established pursuant to Resolution AG-5/70, held its Seventy-fifth Meeting in Cartagena, Colombia, on March 15, 1998.

During the period elapsed since the Thirty-ninth Annual Meeting of the Board of Governors held in Cartagena, Colombia, in March 1998, the Committee held its Seventy-sixth, Seventy-seventh, and Seventy-eighth Meetings in Washington, D.C., on June 24 and 25, November 12 and 13, and December 9, 1998, respectively.

I. Seventy-fifth Meeting (Cartagena, Colombia, March 15, 1998)

Eighth General Increase in the Resources of the Bank. Progress report

- **Report on the operational program, 1994-1997**
- **Enriching an historic partnership. Suggested issues for discussion by the Board of Governors**

The President of the Bank, Mr. Enrique V. Iglesias, gave a brief account of the activities carried out by the Bank during the previous year, offering suggestions and proposals with respect to future Bank activities, which had been inspired by the experience gained in carrying out the Eighth Replenishment activities.

Mr. Iglesias highlighted the following main issues:¹

- (a) evaluation of the fulfillment of the Eighth Replenishment objectives;
- (b) the institution's future work;
- (c) new types of demands facing the institution;
- (d) flexibility of the Bank and its response to emergency situations;
- (e) institutional support loans;
- (f) work with local government and civil society;
- (g) progress achieved in private sector development;
- (h) creation of four working groups of the Board of Executive Directors:
 - budget administration
 - procedures to expedite the Bank's work
 - human resources management
 - evaluation issues.

The Chairman of the Committee turned the floor over to the members of the Committee and other participants for their comments on the IDB operational program for 1994-1997 and on the topic of Enriching an Historic Partnership. Statements were made by the Governors for Guatemala, Mexico, Venezuela, Chile, Brazil, France, Canada, Argentina, Italy, the United States, Denmark, Nicaragua, Uruguay, Norway, and Paraguay.²

The possibility was discussed of convening a meeting of the Committee within the next three months for further follow up on the topic of Enriching an Historic Partnership and it was decided that the issue of the status of concessional funds would be the next item taken up.

The Chairman of the Committee turned the floor over to the Governor for Spain so that he could present the report of the Working Group set up to study the situation of concessional resources.³

¹ See paragraph 3.1 of document CA-400.

² See Annex III of document CA-400.

³ See paragraph 3.6 of document CA-400.

The Committee took note of the remarks made by the Governors for Nicaragua, Bolivia, and Honduras.⁴

Lastly, the Chairman of the Committee recorded a consensus that the Working Group continue working and that the Committee, including observers, would take up the study of the future vision of the Bank. Both groups would have a six-month timetable and would receive technical assistance from the Board of Executive Directors of the Bank, supported as necessary by the Management of the Bank.

II. Seventy-sixth Meeting (Washington, D.C., June 24 and 25, 1998)

Reports by the Chairman of the Committee:

- **Status of concessional resources**
- **Enriching an historic partnership**

The Chairman of the Committee recalled the background of the issue of the concessional resources of the Bank and the mandate conferred upon the Board of Executive Directors in Cartagena to explore the bases in order to move forward on this issue.

The Chairman recognized the fine work done by the Board of Executive Directors over the previous months and indicated that a major effort had been made and that the technical discussions on the matter had been practically completed. She also thanked the Management of the Bank for its cooperation in preparing the information used as the basis for the Working Group discussions.

The Chairman of the Committee gave the floor to Mr. Julio Ángel, Executive Director, in his capacity as Chairman of the Working Group of the Board of Executive Directors, for him to present a report on the progress achieved in the discussions on concessional resources.⁵

The Committee took note of the comments made by the Governors for Jamaica, the United States, France, Nicaragua, Japan, Austria, Canada, Italy, and Brazil, and of the additional comments made by Mr. Ángel.⁶

Following some informal meetings, the Chairman opened the second session. She summarized the conclusions reached during the deliberations with the Governors for the borrowing and nonborrowing countries and submitted to the Committee for consideration a text reflecting the agreements reached by the two groups in very concrete terms.

The Committee expressed agreement on the text, which was as follows:

"Consensus to the effect that the Board of Executive Directors devise a scenario that can resolve the problem of the Bank's concessional resources, which would comprise three elements:

- Establishment of a highly concessional window
- A comprehensive review of concessionality
- Participation by all in a package that reinforces the principle of solidarity

"and that the Board of Executive Directors present its findings to the Committee of the Board of Governors at a meeting to be held in September/October."

"Enriching an historic partnership"

To begin the discussion, the Chairman of the Committee gave the floor to Mr. Julio Ángel, Executive Director and Chairman of the Working Group of the Board of Executive Directors, who presented a report on this matter.⁷

The Chairman proposed that the Committee focus on the issue of private-sector participation and leave the other matters pending until it had more information. She invited the Manager of the Private Sector Department to make a presentation.⁸

⁴ See paragraphs 3.8 to 3.10 of document CA-400.

⁵ See paragraph 2.4 of document CA-405.

⁶ See Annex II of document CA-405.

⁷ See paragraph 3.1 of document CA-405.

⁸ See Annex III of document CA-405.

The Committee took note of Management's presentation and of the comments made by the Governors for Chile, Italy, Canada, Germany, Austria, Japan, Jamaica, the Netherlands, Mexico, Venezuela, Belgium, the United States, Argentina, and Spain.⁹

The Chairman of the Committee summarized the discussion, stating that it indicated that the Governors considered the issue of concessional resources and the content of "Enriching an historic partnership" to be related but not tied to each other, and that therefore, as agreed in Cartagena, they would continue to be treated concurrently but separately. As for the three proposals on the private sector set forth in Annex 1B to document CS-3172-6, the Chairman indicated that Management should continue to examine them in light of the comments made by the Governors.

Note was taken of the statements made by the Governors for Chile and Brazil and the President of the Bank, Mr. Enrique V. Iglesias.¹⁰

III. Seventy-seventh Meeting (Washington, D.C., November 12 and 13, 1998)

Report on the damage caused by Hurricane Mitch in certain countries of Central America and its impact on their social and economic situation

The Chairman of the Committee stressed the magnitude of the damage caused by the hurricane in these countries and noted that the matter had been included on the meeting's agenda at the request of the Governor for Honduras.

The Chairman then turned the floor over to the President of the Bank, Mr. Enrique V. Iglesias, who said that this had been one of the worst natural disasters ever to hit the region and without a doubt the worst one ever to have struck Central America. He went on to say that in addition to the loss of life, the tragedy lay in the loss of physical capital and economic infrastructure, and the serious implications for the medium and long term. The situation was all the more tragic since this region had been through so many tribulations over the years.

Still, the President noted, some comfort could be found in the fact that international public opinion had been so sympathetic to this tragedy. Such a response kindled hopes that the region would receive the necessary assistance.

Aside from addressing the immediate emergency, it was important, said Mr. Iglesias, that the Bank not lose sight of the reconstruction stage, which was every bit as important. He added that this tragedy opened up an opportunity, the chance to rebuild Central America in a creative and more modern way rather than just rebuild it as it was before.

Mr. Miguel Martínez, Manager of Regional Operations Department 2, then presented a report on the actions being carried out by the Bank.¹¹

The Governor for Honduras requested that a video be shown presenting images of the damage caused by Hurricane Mitch, after which she gave an account of the events that had taken place in her country.¹²

The Governor for Nicaragua made a statement expressing his gratitude for the assistance provided to Nicaragua and describing the devastation his country had suffered.¹³

The Governors for the United States, Dominican Republic, Canada, France, Brazil, Venezuela, Italy, Jamaica, Japan, Spain, Guyana, Paraguay, Argentina, Mexico, Bolivia, Chile, and Guatemala each took the floor to express solidarity with the countries affected and to report on their cooperation efforts that were being pursued with those countries.¹⁴

Before moving on to the next item on the agenda, the Chairman noted the Committee's consensus on holding a Consultative Group meeting on December 10 and 11, 1998, to determine the aid that would be needed to mitigate the impact of Hurricane Mitch in Central America.

⁹ See Annex III of document CA-405.

¹⁰ See Annex IV of document CA-405.

¹¹ See paragraph 3.3 of document CA-407.

¹² See paragraph 3.4 of document CA-407.

¹³ See paragraph 3.5 of document CA-407.

¹⁴ See Annex II of document CA-407.

Proposal for action by the Inter-American Development Bank to mitigate the impact of the global financial crisis on Latin America and the Caribbean

The Chairman of the Committee introduced this item by recalling that the deliberations would focus on the agreement to be reached concerning what tools would be used to mitigate the impact of the global financial crisis on Latin America and the Caribbean and concerning the flexibility that would be given to the Board of Executive Directors to approve emergency loans. Mr. Iglesias then took the floor to introduce the topic, and was followed by Mr. Ricardo Hausmann, the Bank's Chief Economist, who reported on the financial situation of international markets, especially in Latin America and the Caribbean.

Mr. Hiroshi Toyoda, Manager of the Private Sector Department, was asked to report to the Governors on how current market conditions were affecting the Bank's private-sector window and how the current proposal concerning that window could help the countries in such circumstances.

Following these presentations, Mr. Iglesias indicated that the Chief Economist's presentation had given a good overview of the nature of the problem that had prompted the Board and Management to call this meeting. He noted that the international situation, attributable to the crisis that had been sparked in Asia and spread through Russia, had affected the region in a variety of ways.

He reported that the International Monetary Fund and the World Bank had asked the IDB to join them in taking measures to help countries already in emergency situations or that should take steps to prevent such situations.

Mr. Iglesias stressed that what was needed was to make funds available to countries that were facing emergency situations or that should take steps to avoid possible runs on their currencies. He noted that these funds should be used for development purposes and would be made available to the countries subject to certain basic conditions: (1) the Bank's ordinary lending program should not be affected but should continue in line with the action programs laid out for the institution; and (2) the Bank's key financial solvency ratios should not be affected.

He went on to say that such actions also needed to be articulated with those of other international agencies; that is to say, they needed to be part of the overall effort and integrated strategy of the Bretton Woods institutions.

The Chairman asked the Governors for their comments on the proposal. Comments were made by the Governors for Bolivia, Ecuador, Chile, Guyana, Guatemala, Peru, Paraguay, Nicaragua, the United States, Mexico, Italy, Japan, Austria, Venezuela, France, Spain, Canada, Argentina, the Netherlands, Belgium, Brazil, Sweden, Norway, Germany, the United Kingdom, and Finland.¹⁵

The Chairman thanked the Governors for their comments and requests for clarification. He then suggested that Management respond to the concerns expressed at a plenary session to be held the following day.

The Chairman called the second session to order and gave the floor to Mr. Iglesias to present Management's reply to the comments made by the Governors.

Mr. Iglesias indicated that hearing the comments of the members of the Committee and the Governors present the day before had been a very useful exercise in that it had allowed those in attendance to become aware of and understand their positions on the proposal. There was consensus, he noted, on the need to set up the proposed emergency facility. In this regard, he felt there was general agreement on the principles embodied in the proposed resolution and on giving the Bank's Board of Executive Directors flexibility to set up this line. He further noted that the Governors had clearly signaled the need to define more clearly some elements that were not spelled out in the original proposal, and accordingly three paragraphs clarifying these points had been drafted.

He explained that the first paragraph embodied the general feeling that all the countries should be eligible to use the line, that such use should be part of a concerted effort with the Bretton Woods institutions, and that the facility should be subject to general guidelines to be approved by the Board. Secondly, as for the definition of an emergency situation, these loans should be disbursed over periods that are substantially shorter than for ordinary loans, with pricing to be determined by the Board, taking into consideration their neutrality with respect to the cost of ordinary loans and maintaining the basic indicators of the institution's financial soundness. Fast disbursement was of the essence in these loans; the respective cost was to be determined by the Board on the basis of two fundamental considerations: the aforementioned neutral impact on cost and the Bank's basic indicators. Thirdly, there would be no negative impact on the ordinary program whatsoever. Management would submit the regular lending program to the Board in accordance with the Eighth Replenishment guidelines, as well as the use of the guarantee system within the parameters approved by the Board.

¹⁵ See Annex III of document CA-407.

The Chairman of the Committee then turned the floor over to the Governors to comment on the proposal. Statements were made by the Governors for Barbados, Peru, Chile, Italy, Mexico, Austria, Belgium, France, Ecuador, the United States, Canada, Bolivia, the Netherlands, Japan, Argentina, Germany, Switzerland, Paraguay, Spain, Brazil, Venezuela, and Guatemala. The President of the Bank also took the floor to respond to some additional concerns that were voiced.¹⁶

The Chairman indicated that, since there was consensus on the proposal, it would be submitted to the Board of Governors for consideration by the process of taking a vote without calling a meeting.

Status of concessional resources. Report of the Chairman of the Working Group

The Chairman turned the floor over to Mr. Julio Ángel, Executive Director and Chairman of the Working Group on Concessional Resources, who presented a report on this matter.¹⁷

The Governor for Guatemala then took the floor to underscore the urgency of this matter, and turned the floor over to the Governor for Nicaragua who requested, on behalf of the governments of Honduras and Nicaragua, and with the support of the other Central American countries, that his comments be recorded in their entirety in the minutes of the present meeting.¹⁸ He asked the Committee, on behalf of Honduras and Nicaragua, to adopt a resolution instructing the Management of the Bank to prepare, in coordination with the countries concerned, a proposed solution, to be presented to the Governors on December 9, with the following elements to address the emergency currently affecting both countries:

1. For already approved loans, that the respective funds be reallocated for immediate disbursement to meet emergency needs, thereby ensuring the necessary liquidity for timely disbursement.
2. For fast-disbursing loans already approved or to be approved, that the conditions for disbursement of the tranches be made more flexible.
3. Considering that both countries have high outstanding balances under active ordinary capital loans (Honduras US\$240 million, Nicaragua US\$150 million), that their debt with the IDB be fast-tracked for reduction and that account be taken of the need for resources to finance the HIPC initiative for Nicaragua and Honduras or any alternative arrangement that could be implemented with the necessary swiftness, given the huge impact of the recent disaster.
4. While the impact of the disaster on the balance of payments and the fiscal accounts of the two countries was being assessed, that the servicing of active IDB loans be substantially alleviated, with a view to taking more permanent debt relief measures and to providing the necessary headroom for action given the great needs generated by the disaster.
5. That sufficient concessional resources be earmarked to meet the needs for reconstruction, in addition to the demand already projected prior to the disaster, including replenishment of projects the funds for which were being reallocated for the emergency.
6. That the Bank support the fast-track preparation of the new operations necessary, independently of the currently available concessional funds.

The Governor for Nicaragua also requested that consideration be given to priority use of any surpluses generated under the new emergency facility approved that morning for the FSO. Lastly, he requested that the Bank ensure close coordination with the International Monetary Fund, the World Bank, and other multilateral and bilateral agencies that had expressed interest in supporting these countries, during preparation of the Emergency Consultative Group for Central America. He asked that the record show their gratitude for the leadership President Iglesias had demonstrated in responding to this emergency.

The Governor for Guyana stressed the urgency of resolving definitively the issue of the replenishment of concessional resources. He emphasized that apart from the countries suffering disasters which required full support, there were other countries that benefited from the use of concessional resources and were also facing serious difficulties imposed by the new international environment. He said that Guyana was the only country in the Caribbean Constituency that benefited from the use of FSO resources. Over the last seven years it had been experiencing growth of about 6.5% on average, but that this year it was likely to have negative growth of 2% and no prospect of improvement in the near term was in sight. The country was experiencing pressures on its foreign currency and the state of underdevelopment was still very relevant.

¹⁶ See Annex IV of document CA-407.

¹⁷ See document CS-3170-13 or Annex V of document CA-407.

¹⁸ See paragraph 5.2 of document CA-407.

The Governors for the Dominican Republic, France, Chile, and the United Kingdom then took the floor to second the motions made.

The Governor for the United States enlarged upon this issue, indicating that the decision to accelerate the FSO lending for the current year and the following year's programs had to be considered within the FSO discussions because of the direct impact on liquidity. Precisely what that impact was, was unclear at that point and a direct input and response from the Finance Department would be needed in that regard. In terms of debt, he indicated that the discussions had been consistently trying to address—before the hurricane—the Nicaraguan HIPC resources requirement, but that a range of other factors had arisen, such as the Honduran situation, that needed to be looked at as well. The intention was to do everything possible to get the maximum financing for concessional resources. Lastly, he expressed hope that the President would be helpful in making it the finance office's top priority in the next few weeks to do the necessary calculations, so that they could be brought to the meeting room with a final solution on December 9th.

The Governors for Venezuela, Sweden, Italy, Bolivia, and Austria supported the foregoing considerations. Mr. Iglesias and Mr. Ángel offered some additional clarifications.

The Chairman of the Committee recorded a consensus that the Committee meet on December 9, 1998, to discuss the issue of concessional resources.

IV. Seventy-eighth Meeting (Washington, D.C., December 9, 1998)

Report by the Chairman of the Committee. Status of concessional resources

To begin consideration of this matter, at the invitation of the Chairman, the President of the Bank, Mr. Enrique V. Iglesias, made a presentation, in which he expressed his confidence that the present meeting would mark a turning point in the search for a solution to the problem of concessional resources, on which the Governors had been working hard for nearly two years.

He indicated that a group from the Board of Executive Directors had been working intensively to devise a solution to the problem, and that their efforts had provided basic elements for identifying the nature of the problem. He went on to say that bilateral meetings had been held among countries to examine possible alternatives and that the joint effort had been truly impressive.

Mr. Iglesias stressed that this meeting was taking place on the eve of a very important meeting for Latin America and the Caribbean and above all for Central America, to review the dramatic situation in the Central American countries devastated by Hurricane Mitch as well as in the Dominican Republic and Haiti, which had also suffered serious hurricane damage.

He mentioned the need to seek a comprehensive and lasting solution to the lack of concessional resources, reiterating his plea that Governors take into account the special circumstances that were occurring and that every effort be made to find a solution to the problem.

He pointed out that a comprehensive solution was being proposed to make it possible to address the numerous demands to which the Bank needed to respond at this time through a joint effort. These demands concerned replenishment of FSO resources, the problems of the Intermediate Financing Facility, the demand for technical cooperation, and the very strong demands in connection with the HIPC initiative for Nicaragua and—if approved by the International Monetary Fund and the World Bank—for Honduras. He said the solution being proposed was a medium-term one so that the matter would not have to be revisited for another decade and would also help strengthen solidarity among the countries since the discussion that had proven so difficult and time-consuming over the past few years could be wound up.

Secondly, Mr. Iglesias indicated that the solution adopted must ensure observance of the principle that the net income of the Bank be reserved for the functions established by its Charter. The proposed alternative not only sought to resolve the problem through the availability of local currency resources held by the countries but also was a comprehensive one that preserved income on the Bank's capital for its specific purposes, while also allowing some Bank resources that had been accumulated over the years to be used.

He indicated that these local-currency resources would be converted over a long enough period so as not to become an onerous burden on the countries in the region. This conversion would mean significant funds being relinquished by the borrowing countries. The local-currency funds existed as a result of agreements reached in the past and, although conditions had now changed, their conversion was a generous contribution to the solution.

Mr. Iglesias went on to say that the proposed resolution also addressed other issues that had led to lengthy discussions over the past year. The first was an adjustment in the base for the 35% and 65% targets for distribution of Bank lending among country groups, to help fulfill the Governors' wishes that access to loan resources be protected for low-income countries, as well as the use of resources for direct lending to the private sector, whereby a cap of 5% of the entire active Bank portfolio, not including emergency loans, was proposed as well as some institutional adjustments to better organize the number of departments that report to the Executive Vice President's Office.

The Governors for Guatemala, Canada, France, Japan, Italy, Guyana, Chile, Mexico, Venezuela, Argentina, Nicaragua, Honduras, Peru, the United States, Brazil, and Bolivia took the floor to comment on this issue.¹⁹

Bearing in mind the comments made by the Governors, and the fact that certain aspects of the proposal under consideration still needed to be clarified, the Chairman of the Committee suggested that the deliberations be continued in a more informal and limited setting. A working group was thus to be made up exclusively of the 14 members of the Committee.

The Chairman of the Committee called the Second Plenary Session to order and thanked all the Governors for the support and flexibility they had shown during the informal meetings. He then summarized the conclusions of the discussions and submitted to the Committee for consideration a text reflecting the agreements reached in very concrete terms.

The Committee expressed agreement with the text, which is transcribed below:²⁰ "Agreement reached at the Seventy-eighth Meeting of the Committee of the Board of Governors (December 9, 1998)

1. Brazil makes available 80% (US\$718 million) of local currency. All other countries except for D-2 countries make available 65% (US\$1,435 million) of local currency.
2. Taking into account availability, types and sources of resources, and the agreed lending program, conversion flows will be established by the Board of Executive Directors in consultation with Management.
3. Total D-2 country resources will be converted after the year 2009. In the exceptional event that the D-2 countries are not able to fulfill this commitment, non-borrowing countries will undertake to find a solution to the problem without further commitment by borrowing countries.
4. Each non-borrowing country will make its best efforts to accelerate payment of its flow of FSO convertible-currency resources under the Eighth General Increase in Resources.
5. The agreement implies acceptance by the Board of Governors that the net income of the Bank's Ordinary Capital, beyond that provided for in the Eighth Replenishment agreement, will not be allocated to the FSO or HIPC.
6. The remaining local-currency resources will be available to the issuing countries in accordance with the applicable regulations.
7. The non-borrowing countries undertake to make their best efforts in contributing to the Fund for Reconstruction of Central America, on a voluntary basis.
8. The IDB contribution to the HIPC facility for Honduras, if eligible, will be financed from FSO resources.
9. The proposals in document CS-3170-14 regarding "Improving the Bank's capacity for effective management", "Country distribution of lending", and "Lending to the private sector" are agreed.
10. The IFF, FSO, and TC financial program, and HIPC for Nicaragua, as proposed for the years 2000-2008, and the US\$100 million contribution to finance reconstruction for Central America, as set forth in document CS-3170-14, are agreed."

The Chairman of the Committee indicated that since there was a consensus on the text, it would be submitted together with the proposal to the Board of Governors for consideration by the procedure for taking a vote without calling a meeting.

Lastly, the President of the Bank highlighted the historic significance of the agreements reached, which concluded negotiations that had gone on for over two years.

Other distribution:

Channels of communication
Executive Directors
Managers
Representatives

¹⁹ See paragraphs 2.3 to 2.18 of document CA-408.

²⁰ See paragraph 2.23 of document CA-408.

**REPORT OF THE COMMITTEE OF THE IIC BOARD OF GOVERNORS
ON ITS ACTIVITIES SINCE THE LAST ANNUAL MEETING**

REPORT 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 by Resolution CII/AG-3/92, held its Fifteenth Meeting in Cartagena, Colombia, on March 14, 1998.

In the interval since that meeting, the Committee has met three times at the Corporation's headquarters in Washington, D.C., on November 13, 1998, December 9, 1998, and February 9, 1999.

I. Fifteenth Meeting (Cartagena, Colombia, March 14, 1998)

Action plan for the Corporation for the period 1995 to 1997, and status of IIC resources. Progress report

The Chairman of the Board of Executive Directors, Mr. Enrique V. Iglesias, reported that 1997 had been a very satisfactory year for the Corporation. The number of operations had risen 25% over 1996 and the total volume of US\$150 million was nearly double the previous year's. Disbursements were up by 20%, gains on the sale of equity investments were up 38%, and dividends had increased threefold. Net income stood at roughly US\$16 million, of which US\$13 million was allocated to the reserves. These results had been achieved with a very reduced staff of some 60 employees (one half the staff level of four years previously), and administrative costs had remained stable for four consecutive years.

Resources, he noted, continued to be the core issue, since the Corporation was still operating at its original level of capitalization. A special effort would need to be made in this area, since the only other option would be to continue operating on the basis of the gearing ratio; this would seriously limit the IIC's ability to channel equity investments more broadly to small and medium-sized companies, as called for under its mandate. The greater risk entailed in working with these companies can only be mitigated through a higher volume of operations, given that the constraints on the IIC's action capacity make its portfolio more vulnerable to the risks taken.

Mr. Iglesias also mentioned the matter of coordination between the Corporation, the Inter-American Development Bank, and the Multilateral Investment Fund, which has a specific facility (Window 3) for microenterprise and small business.

Work should focus, he reaffirmed, on making genuine progress in negotiations on a capital increase, recalling that the Committee, at its 1997 meeting in Washington, had agreed that the working group of the Board of Executive Directors, chaired by Mr. Pineda, the Executive Director for Mexico, should put in place—in line with the methodology established by the Governors—a consultation mechanism to define possible alternatives for an agreement on the first general increase in resources of the institution.

Mr. Iglesias encouraged the Corporation to welcome new regional members as well as other countries that are members of the IDB.

The Corporation's General Manager *ad interim*, Mr. John Rahming, then gave a report in which he noted that, throughout 1997, the Corporation had fulfilled its mandate to assist small and medium-sized businesses in Latin America and the Caribbean.

The Corporation, he noted, currently had a diversified portfolio managed in keeping with strict guidelines set by the Board to mitigate financial and operating risks. The practice of working with equity investment funds enabled the IIC to reach more than 1,000 small and medium-sized companies and leveraged its resources many times over to the benefit of the region's private sector, especially smaller companies. Equity investment funds had been one of the priorities identified in the action plan approved by the Governors at the 1995 Annual Meeting in Jerusalem, and the Corporation now had 37 such funds—up from 7 at year-end 1994. These funds were currently at the active investment or fund-raising stage. Of the total capitalization of over US\$1 billion, IIC resources represented US\$100 million for a leverage ratio of 10 to 1. The investment funds had already made more than 76 investments for a total of US\$420 million.

After a decade of economic stagnation, real growth in Latin America and the Caribbean was expected to reach 5% per annum in the final four years of the decade. Growth would be fanned in part by the incipient free-market sector that was emerging in countries across the region. To fully realize the potential this represented, companies would increasingly require equity capital, loans on reasonable terms, and assistance in developing efficient production, marketing, and financing strategies. To achieve this, the region would need private investment flows willing to commit for the long term, and it needed institutions capable of providing and catalyzing these flows while shaping their developmental impact.

In closing, Mr. Rahming noted that a capital increase would allow the Corporation to continue attracting private capital to meet the growing finance needs of the region's small and medium-sized enterprises. It would therefore be important to make recommendations, without further delay, on the amount of the general increase in resources to be submitted for consideration by the Governors in the near future.

The Governors for Mexico, Venezuela, Italy, Colombia, Brazil, Switzerland, the United States, Argentina, and Paraguay then took the floor. Their statements appear as Annex III to document CII/CA-52.

After an exchange of views, the Committee agreed that consideration of the matter would continue in the Budget, Financial Policies, and Audit Committee of the Corporation's Board of Executive Directors and that a document containing additional information and recommendations would be presented. To this end, the Governors were asked to submit their suggestions and possible alternatives that could provide guidance for the working group.

II. Sixteenth Meeting (Washington, D.C., November 13, 1998)

General Increase in the Resources of the Inter-American Investment Corporation. Progress report

The Chairman of the Board of Executive Directors, **Mr. Enrique V. Iglesias**, recalled that this matter had been discussed extensively by the Executive Directors and that the Governors had received the document known as the ten-year plan for the Corporation. He added that this initiative, which was already an important one six months earlier, had become even more so, to the extent that the situation on international markets made it all the more imperative to have institutions such as this one to help strengthen local enterprises in the region, while promoting participation and cofinancing by international capital.

The private sector, he noted, was suffering considerably from the impact of the financial crisis, and political will needed to be mobilized rapidly in order to give the IIC the increased resources it needed to be much more active in the region's time of difficulty.

The General Manager *ad interim*, **Mr. John Rahming**, then took the floor to report on recent developments in conjunction with the devastation caused by Hurricane Mitch and the coordination of efforts by the IIC, the Bank's private-sector activities, and the MIF.

He offered an overview of the Corporation's work throughout 1998, noting that it continued to fulfill its mandate of assisting small and medium-sized companies in Latin America and the Caribbean. Twenty-nine projects were expected to be approved in the current year (compared with 25 in 1997), for a total of US\$223 million (compared with US\$150 million in 1997). Fifty per cent of those resources would be channeled to Group C and D countries, and disbursements for 1998 were 50% higher than in 1997. The IIC now had a diversified portfolio that was being managed in such a way as to mitigate financial and operating risks; it was divided into the following main sectors: financial services, which accounted for one fourth of the institution's active operations and enabled it to make financing available to smaller companies; the manufacturing sector (25%); agribusiness (15%); venture-capital funds (10%); small- and medium-scale infrastructure (10%); and mining, fisheries, and tourism (15%).

Seventy-two financial intermediaries had received more than US\$381 million in lending from the IIC and US\$284 million in cofinancing.

Given the underdeveloped nature of many of the region's capital markets, Mr. Rahming noted, the IIC sponsors private equity funds and direct investments in markets that may not be targeted by fund managers, as an appropriate mechanism to cover part of the equity requirements of small and medium-sized companies. With a broader capital base, the Corporation could better address these equity needs and, through leveraging, grant more loans.

The Blueprint 2000 proposes that the Corporation increase its total funding sixfold over a 10-year period, compared to its first decade of operations, to reach more than 10,000 small and medium-sized businesses.

Mr. Rahming pointed out that the Corporation had virtually depleted the initial capital contributed by the member countries. Although it was in a position to continue granting loans, it needed a meaningful capital increase in order to continue meeting the equity needs of the region's small and medium-sized companies. The present meeting, he noted, offered an opportunity to gather comments, guidance, and suggestions for negotiation and approval by the current shareholders and the six, seven, or eight new shareholders that were seeking to enter; the trigger points for various voting issues and the capital pay-in period also needed to be negotiated. In closing, he stated that Management stood ready to provide any necessary information and to assist the Executive Directors in this process so as to facilitate final decisions by the Governors.

Mr. Moisés Pineda, Executive Director, in his capacity as **Chairman of the Budget, Financial Policies, and Audit Committee**, then took the floor. In his report, he said that a 10-year period had been identified as the term after which the Corporation could examine the possibility of a mixed capital stock structure with private capital and, if deemed appropriate, step up its pace of activity. The amount of US\$500 million had been established as the figure that would enable the Corporation to become self-financing in the long term.

Areas had been identified in which changes needed to be made in the operation of the Corporation in order to make it more efficient, flexible, and competitive, and to mitigate the risks inherent in the market it serves. Information disclosure needed to be more transparent, and strict standards for environmental and labor protection should remain in place. The

new shareholding structure had been defined as it would stand after the capital increase and the admission of new members, and timetables had been drawn up for payments over periods other than the original four-year period.

Mr. Pineda noted that any comments and guidance received from the Governors at the meeting would be very helpful for the working group to continue its work. Following the meeting of the Governors, the working group would focus on framing specific recommendations as to the future shareholding structure and that of the countries that had applied for membership or might do so in the future; these recommendations could be assessed and discussed at the next Committee meeting.

The Governors for the United States, France, Spain, Guatemala, Guyana, Venezuela, Mexico, Argentina, the Netherlands, and Chile then took the floor. Their statements are attached as Annex III to document CII/CA-62.

After an exchange of views, the Committee agreed that consideration of this matter would continue in the Budget, Financial Policies, and Audit Committee of the Corporation's Board of Executive Directors and that a document containing additional information and recommendations from the meeting would be presented for consideration at a meeting of the Committee of the Board of Governors to be held in early December 1998.

III. Seventeenth Meeting (Washington, D.C., December 9, 1998)

General Increase in the Resources of the Inter-American Investment Corporation. Progress report

The Chairman of the Board of Executive Directors reported on the progress of negotiations under way with regard to the general increase in resources of the Corporation (documents CII/CA-53 and CII/CA-53-1). He proposed that internal discussions be continued in January 1999 and a meeting of the Committee be scheduled for early February 1999.

IV. Eighteenth Meeting (Washington, D.C., February 9, 1999)

General Increase in the Resources of the Inter-American Investment Corporation. Progress report

The Chairman of the Board of Executive Directors reported on the progress of negotiations under way with regard to the general increase in resources of the Corporation (documents CII/CA-53 and CII/CA-53-1). The Corporation's General Manager then shared some comments on the issue, after which the floor was turned over to the Governors. The Chairman of the Committee subsequently decided to convene a working group to continue the deliberations.

Following an extensive exchange of views, the Chairman of the Committee recalled that it had been agreed to recommend a US\$500 million increase in the Corporation's capital for a ten-year program, subject to—but not conditional on—a midterm review of the institution's performance in deploying its resources and complying with its operating policies, via mechanisms to be agreed during the upcoming negotiations in Paris.

Another element of the agreement concerned the commitment that the capital increase be paid in over eight years. It was proposed that the new members pay their contributions over a shorter period of time than the Corporation's existing member countries. Other potential arrangements were also possible, with the participation of Canada, to facilitate payment by certain countries.

The Chairman of the Committee noted that there were two matters still under consideration: (i) the distribution of the capital and its allocation among existing and new shareholders, and (ii) the possible increase in the number of chairs on the Board of Executive Directors. In this regard, a formula submitted for consideration by the Governors had as its underlying principle that of burden-sharing dilution.

The group of Latin American and Caribbean countries (GRULAC) had offered to decrease its shareholding to 51%. It was suggested that GRULAC consider the possibility of a greater decrease, on the understanding that its shareholding would be less than 51% but never below 50%. This shareholding cession—and the cession that might be made by other countries and groups of countries—would make the necessary room for allowing the entry of Canada and the other European countries.

The United States had also expressed its willingness to decrease its shareholding by a percentage that was still under discussion but would be significant and sufficient to make—with the shareholding cessions to be made by the other member countries—room in the institution's capital for the entry of new member countries and for the possible readjustment of the shareholdings of existing members such as Japan. The United States had indicated that the possible decrease in its shareholding percentage should be accompanied by an increase of the percentage of votes required for approving future capital increases, in accordance with the Charter and the Corporation's by-laws.

Also, and in support of the efforts on the part of GRULAC and the United States, it was proposed that the European countries that were currently members of the Corporation also cede shareholdings, which could be on the order of 2% of the capital, and restructure their participation to allow the entry of new members.

It was felt that this formula would have several virtues: (i) it took into account the concern expressed by many Governors that the effort to allow the entry of new shareholders be shared by all the members; (ii) it made it possible to adjust the participation of certain countries in the institution's capital; and (iii) it satisfied the interest expressed by Canada in entering with a significant shareholding.

As for the possible creation of new chairs on the IIC Board, during the discussions most of the countries had favored the possibility of creating a single additional chair. The composition of the chair was to be defined by the Governors at the upcoming meeting in Paris, taking into consideration the proposal that the country to which the chair was assigned consider making an additional contribution to the IDB Group's effort to strengthen the region's private sector.

The Chairman of the Committee reported that the working group would continue its deliberations starting at 10:00 a.m. on Friday, March 12, in Paris, so as to reach solutions that would enable an agreement on the IIC's capital increase, which had been the object of such prolonged negotiations.

Other distribution:

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Managers
IDB Representatives

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