



ANNUAL MEETING OF THE BOARDS OF GOVERNORS

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**ADDRESS BY THE TEMPORARY ALTERNATE GOVERNOR FOR ITALY
AT THE SECOND PLENARY SESSION**

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1. On behalf of the Italian Government, I would like to thank the Government and the people of Brazil, and particularly the State of Ceará and the City of Fortaleza for their warm and generous hospitality. I would also like to congratulate the Bank's Management and staff for the excellent arrangements for this meeting.

The international scenario and Latin America and the Caribbean after September 11

2. 2001 was a very difficult year. Economic activity worldwide weakened even before September 11. The terrorist attacks and their aftermath further deepened risks and uncertainties.

3. The initiatives taken by the international community immediately after September 11 have eased some of the negative effects on the world economy. Recovery is now expected to accelerate, both in Europe and in the United States.

4. But the world's poorest nations are under threat of being further marginalized. After September 11, the IMF revised downwards growth forecasts for Latin America by 2.7 per cent, a revision that is more than double that for industrial countries and also greater than that for Africa (-0.6 per cent), Asia (-0.8 per cent) or the Middle East (-1.8 per cent).

5. Although contagion has been limited until now, Argentina's crisis has further added to the structural weaknesses of the region.

6. For Latin America and the Caribbean, this new century has started much as the previous decade. As you recall (quoting from the IDB Annual Report), the region recorded in the 1990s the worst growth performance among the world's main regions, with a 3.3 per cent average growth rate, against 5.1 per cent in East Asia, 4.0 per cent in the Middle East, 5.2 per cent in the rest of Asia, and 3.5 per cent in Eastern Europe. In per capita terms, the income of Latin Americans rose by only 1.5 per cent a year over the past decade, compared to 3.3 per

cent in East Asia, 3.5 per cent in the rest of Asia, and 2.7 per cent in Eastern Europe. Only Africa and the Middle East did worse, with 0.5 per cent and 1.2 per cent respectively.

7. Two main factors can be singled out for such performance: low educational levels and the poor quality of public institutions. Quoting again from the IDB Annual Report, the average educational level of the region's workforce grew only 1.5 per cent per annum in the 1990s, compared with a 2.5 per cent increase in South Asia, and higher education is still concentrated in a relatively small group of the population. This is one of the main reasons for the high income inequality. If there are no doubts that economic growth is key for reducing poverty, it is also true that income inequality is a major obstacle to economic growth.

8. The weak institutional framework remains a major hardship. To quote the 2001 Report on Economic and Social Progress edited by the IDB, policy instability is regarded as a major problem for 38 per cent of business people in Latin America, against 25 per cent in Africa, 20 per cent in Asia, and 14 per cent in the developed world.

The fight against poverty

9. The fight against poverty and social inequity requires a collective commitment by all stakeholders: Latin American countries, industrial countries, international institutions, especially the IDB.

10. Countries in the region have the primary responsibility for fighting poverty more effectively. We know what is needed: sound macroeconomic policies; structural reforms; a strong legal and regulatory framework; fight against corruption-the International Monetary Fund (IMF), the World Bank, and the IDB remind us of this all the time. We have to deliver.

11. Industrial countries also have major responsibilities. The first test of credibility in the fight against poverty lies in our ability to open up our markets and phase out trade-distorting subsidies in sectors where developing countries have a comparative advantage. The European Union has a leading role to play in this respect, since it imports more than half of developing countries' exports. Last year, the European Union decided to fully open its markets to the poor countries' exports, except for arms. We encourage the other industrial countries to follow this initiative. The second test of our commitment is to increase official development assistance (ODA) flows to help developing countries fighting poverty. European Union countries have committed to increase the volume of aid to 0.7 per cent of GDP in the near future. We need not only more aid, but also better quality of aid: a more effective use of resources.

12. Last, but not least, the international financial institutions, and in particular the IDB, have a crucial role to play in the fight against poverty in Latin America. However, these institutions have to be fully equipped to perform their tasks more effectively.

The MDB reform process and the IDB

13. In the course of last year, we discussed with the management of multilateral development banks (MDBs) and with other shareholders ways to improve their effectiveness and efficiency. These discussions led to concrete proposals and commitments that are contained in the G7 Finance Ministers Report on MDB reform, released in July last year in

Rome. Six areas were highlighted in which we agreed to take major steps to improve efficiency, namely: coordination, good governance, lending instruments and pricing review, global public goods, financial sector reform and, finally, internal governance.

14. After eight months, we can assess together the main achievements in these areas.

1. *Coordination*

15. On coordination among MDBs, the report called for strengthening the links between MDBs' country strategies within the development framework. The Memorandum of Understanding between the World Bank and the IDB is an important first step in this direction. Now we expect further progress in the alignment of country strategies. We also expect in the course of this year improvements in prioritizing and accelerating the harmonization process.

2. *Good governance*

16. On governance, there is broad agreement that country strategies should also include a review of the country's governance, with particular focus on public sector management, accountability and anti-corruption measures. Public sector management and accountability are already included as priorities in the newly-prepared country papers. More attention can nevertheless be given in IDB strategic documents to the rule of law and to measures to fight corruption. Furthermore, we suggest that the IDB's lending activity increase the focus on good performers, thus creating the right incentives, ensuring the most effective use of scarce resources and enhancing the development effectiveness of the Bank's operations.

3. *Lending instruments and pricing review*

17. We all agree that the MDBs, and the IDB in particular, should focus more and more on operations targeted at poverty reduction and enhance the development impact of our scarce resources. This calls for greater selectivity in operating in sectors where access to private capital is improving. MDBs have also agreed to review their lending instruments and pricing policies. We thus welcome the recent agreement by the IDB Governors to enhance the Bank's capability to respond to the increased needs of the member countries, in particular by diversifying its lending tools. This will allow the IDB to broaden the means to support the region's development, with due attention to the financial soundness of the Bank. In order to be effective, this new framework should be implemented hand-in-hand with the establishment of clear objectives and measurable indicators and the strengthening of the monitoring and evaluation function of the Bank. Indeed, we would not want the Bank to transform itself into financing primarily budget and balance-of-payment needs. Priority should always be given to poverty reduction.

4. *Global public goods*

18. Global public goods have a strong impact on development and poverty reduction. The main priorities are fighting infectious diseases, promoting environmental improvement, facilitating trade and supporting financial stability. The IDB has already launched a number of initiatives in the areas of infectious diseases, environmental protection and regional integration. We very much welcome these initiatives. We will work closely with the

Management to identify further areas where the IDB can provide value added, in close coordination with the World Bank.

5. *Financial sector reform*

19. The IDB, as other MDBs, has been asked to play a more proactive role in assisting borrowers, especially low-income countries, in developing institutional capacity and appropriate strategies to meet international codes and standards, including the Financial Action Task Force (FATF) anti-money laundering standards. Some progress has been made to enhance cooperation with FATF, but more can be done. We also need to be assured that by the end of this year all country strategies incorporate financial sector issues and consider measures to meet international codes and standards.

6. *Internal governance*

20. Finally: internal governance of the MDBs. Accountability and transparency are crucial to strengthen MDBs' credibility in the eyes of our parliaments, of civil society, of all stakeholders in general. Strengthening compliance mechanisms, ensuring timely disclosure, establishing a more transparent budget process, improving effective circulation of documents, and reviewing internal organization: these are the areas where we agreed to work further together. We appreciate Management's efforts aimed at certifying that IDB-financed operations have a clear development impact, aligning internal processes, procedures and incentives towards the attainment of results. Further efforts can be made on improving the monitoring and the evaluation functions of the Bank. One way to further improve these functions could be to set up a Development Assessment Unit with the task of carefully assessing the development impact of each single project. Another area where improvements can be made is the budget process, with a view to give shareholders control over compliance between the institutional priorities and the allocation of resources.

The role of the private sector

21. Some additional words on the IDB's critical role in promoting the private sector.

22. We welcome the study of the External Advisory Group chaired by President Gurría on the future role of the IDB. It contains many stimulating ideas, in particular on the role of the private sector, that are consistent with the reform agenda that we have launched. These ideas need to be seriously considered and pursued further.

23. The investment climate in the region needs to improve dramatically. One way is to foster the development of small and medium-size enterprises, which can be instrumental in promoting economic growth and alleviating poverty. This requires a sensible governance system and proper infrastructures that allow private entrepreneurs to emerge and operate effectively. In this context, the IDB has a unique opportunity for strengthening its catalytic role to help countries develop an institutional and regulatory environment that can promote favorable conditions for private sector investments.

Conclusion

24. Mr. President, this first decade of the third millennium can mark a reversal in the declining trend experienced by Latin America and the Caribbean at the end of the last century. It is our responsibility not only to wish so, but to achieve it. We are confident that under your leadership the IDB will continue to reform itself and strengthen further its role in the region. As a shareholder of this institution, we will continue to support the policies and the strategies of this Bank and we will do our best to work with you and the other shareholders to improve the capacity of the Bank.

25. Mr. President, in wishing the Bank success in this coming year, let me conclude that it will be an honor for the Italian authorities to host the next annual meeting in Milan in 2003.