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On behalf of Argentina, Bolivia , Chile, Paraguay, Peru, Uruguay

Statement by the Honorable Hernán Lorenzino
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Speaking on behalf of the Southern Cone Countries of Latin America
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I. The Global Economy

Global economic prospects have improved and although the immediate threats identified in the previous World Economic Outlook (WEO) have been dealt with somewhat, we are less optimistic for the near-term outlook. Recovery remains elusive and it is not clear whether in the fifth year since the beginning of the crisis there really is a light at the end of the tunnel. The risks associated with excessive short-term fiscal tightening in the United States, political uncertainty and the increasing risk of a long-term crisis in the euro zone and, the very recent deep financial turmoil in Cyprus pose new challenges to economic recovery and financial stability.

On the one hand, important brakes remain in place in advanced economies (AEs), including weak corporate and household balance sheets, tight credit conditions, and poor confidence. We are aware that there are no silver bullets but, more worryingly, there might simply be no bullets at all, such that, economies will become less manageable should new problems appear. On the other hand, it is striking that both stock and equities appear rich in U.S. markets, and a correction in either would clearly add to volatility and uncertainty, further undermining consumption, investment, and economic growth. The last wave of tensions in the euro zone showed how fragile the (OMT and program-driven) recently lower volatility truly is, particularly to policy missteps. The current unprecedented crisis in Cyprus, both in terms of its magnitude, as well as the policies needed to contain it, shows once again the substantial challenges that the euro area faces to preserve the common currency. Solvency and competitiveness issues require profound economic and institutional changes, but the pace of progress appears to remain too slow to decisively turn the corner.

Global growth, as projected by the recent WEO for 2013, is slightly higher than it was for 2012, with a three-speed global recovery emerging. The output in the euro countries is projected to be negative, as negative growth rate is projected for 8 of the 17 AEs of the area, and other AEs, like the U.S. and Japan, are decelerating their growth. Last year, when monetary and sovereign policies were announced by the European and Japanese central banks and by the FED, calm returned to the markets, but the slowdown of these economies is not an encouraging sign; consequently, monetary easing and the fall of demand spillover pressures are transmitted to the rest of the world affecting the growth prospects for emerging market and developing countries (EMDCs) and low-income countries (LICs). All this implies greater risks of broad contagion to bystanders; for these reasons, growth prospects for South America for 2013 have increased by only 0.5 percent with regards to 2012.

Although in EMDCs the expansion of output is expected to become more broad-based and accelerate steadily, risks remain. On the one hand, this baseline scenario assumes that most of the slowdown in large emerging economies during 2012 was cyclical, and thus one should expect a quick rebound, thanks to recent policy stimuli and its concomitant effect in investment and consumption. This, however, is difficult to square with a process of continued deflation in AEs and projected lower commodity prices. Therefore, notwithstanding the overall positive tone in emerging markets today, the authorities should continue to press ahead for more investments and the availability of long-term investment finance, particularly in infrastructure and education, to increase potential output and maintain the process of economic expansion and poverty reduction.

The Managing Director's Global Policy Agenda (GPA)[1] takes stock of the policy priorities outlined in the last GPA (October 2012) for the membership in order to secure the recovery and anchor the future. We note in the document on Assessment of Membership that although the member countries have implemented many of their commitments, particularly emerging market economies and LICs, Middle East and North African (MENA) countries due to their social and political situation and the nature of its transition process, need more time to implement them, while the AEs have fallen behind their needed commitments. We believe that, to avoid unevenhandedness, as the IEO recommended[2], the IMF should strengthen incentives to "speak truth to power" in AEs.

If a summary score were done on "key IMF deliverables", it would be closer to that of AEs than emerging markets or LICs. It has 71 percent of deliverables underway, 7 percent delayed and only 22 percent completed. Besides some work considered generously, such as that completed, like the advances in capital flows, others like the work on subsidies that is in process, shows the outcomes are not clear when AEs subsidies are not taken into account in the policy recommendations. Another important deliverable project, supported by several countries, is the need for an assessment of outcomes of lending programs in recent years.

The Fund identifies several risks to the system. Public finances remain unsustainable in the U.S.; there is a need for urgent progress in reforms to deal with the vulnerabilities in the financial system and the euro zone, as seen in Cyprus. There are fiscal risks in Japan, due to the short-term fiscal stimulus and the rapid expansion of the financial system in China which should be addressed through more regulation and supervision. Concerns also arise on the spillovers from loose and unconventional monetary policy in AEs and the impact on EMDCs of large inflows of short-term capital. The risk of "adjustment fatigue", as the IMF calls the social and political tensions created by hard conditionalities, and unfair distribution of the burden imposed on several countries, particularly those in the European periphery by the extraordinary adjustment and the austerity measures which has led to the strong fall of output and an increase of unemployment, has added unexpected problems to those they already face, i.e., the fall in tax revenues that led to increased fiscal deficits. Greece, after five years of a fall in GDP by an average yearly rate of -4.3 percent is projected to continue to fall by -4.2 percent in 2013. Would it be worse without IMF support?

[1] (IMFC/Doc/27/13/2)
[2] See IEO Report (2011) "IMF Performance in the Run-up to the Financial and Economic Crisis": IMF Surveillance in 2004-07, Chapter 5, page 22.

II. Invigorating a Sustainable Recovery

In an interlinked world, vulnerabilities in AEs that can spread to other countries need collective and cooperative actions at the international level to restore the bases of strong growth with social inclusion. All countries have a responsibility to build a stronger and more resilient world economy and a stable international monetary and financial system, but the level of commitment and responsibilities are different among AEs, and EMDCs, including LICs.

Membership: AEs, EMDCs, LICs and MENA

Since 2010 when the ashes of the crisis were still hot, the Fund's advice to AEs was: adjustment and fiscal consolidation. In the 2013 GPA, the advice continues to be short-term adjustment and medium-term fiscal consolidation. Both policies counteract the domestic benefits of accommodative monetary policy and are counterproductive to a growth strategy, with recession pressures, as the excess money tends to flow out of the country producing negative cross border spillovers. That is why these policy responses by AEs at the domestic level should be carefully analyzed and all types of spillovers which could destabilize other economies should be avoided.

EMDCs should not lose momentum in invigorating a sustainable recovery, although several of them, particularly the major emerging economies, are facing an economic slowdown whose origin has to do more with the problems in AEs than with domestic problems. EMDCs are in a good position due to the benefits of the macroeconomic and structural policies applied, growth rates remaining higher than the global average, the public debt being moderate or decreasing, and many of these countries could provide fiscal support, not only to continue helping to sustain global economic recovery, but also to withstand a way out of the current situation. Tighter regulation, supervision and control will help protect against potential financial stability risks, large capital inflows, high asset prices, rising corporate leverage and foreign exchange exposure.

Investing in infrastructure is a key element for the economic development of EMDCs. This policy could also help advanced countries—especially now as their growth prospects are weak—to restore their economic prospects. Infrastructure projects tend to produce movements and linkages benefiting the entire economy. It creates jobs, eases transportation and logistical arrangements (which in turn facilitate exports); thus, it produces many positive externalities.

Robust growth in LICs should be sustained as a way to meet infrastructure and social needs.

The MENA region is dealing with particular difficulties; it needs time to advance in solving the several problems facing the region. Resources are needed to provide transfers to the poor, such as productive and infrastructure investments which create growth and employment. Donors should support the countries of the region, with external official finance and trade access.

The Fund´s Role

With regard to accommodative monetary policy, fiscal adjustment, the debt ceiling and consolidation in AEs, the Fund should not only continue analyzing the global benefits and risks of them but should make AEs aware of the tsunami effect of cross border spillovers and advise EMDCs on defensive policies.

In the case of Europe, the Fund should not only assist on fiscal issues, it should help develop a framework for taxing the financial sector. At the same time, the Fund should continue with repair and reform as proposed, and it also needs to carefully and deeply assess the outcomes of the programs in operation to align them with a sustainable recovery. These programs imposed policy conditionalities and reform strategies on certain peripheral European countries, which are worsening the economic situation and unemployment levels while leading to unsustainable debt paths and social failure. These programs are in many ways a repetition of the IMF's mistaken policy conditionalities applied to many countries in the 90s that ended in economic crisis. Unfortunately, the institution seems to have forgotten some of the lessons from the Asian and Latin American crises.

Moreover, the Fund should be clearer in its messages to the membership; it needs to build more coherence between its surveillance activities, mainly with messages that stem from the WEO and other IMF publications, and its lending role. In particular, the IMF has been rightly pointing out in recent WEOs that the policy mix implemented in AEs after the crisis, particularly in the euro area, has been detrimental to recovery. It has also identified that policy-makers and IMF staff have been excessively and continuously optimistic on program countries' forecasts. More recently, Box 1.1 (The Great Divergence Of Policies) in the Spring 2013 WEO once again rightly identifies that fiscal policies implemented after the crisis have been overly conservative in AEs, compared to policy responses to past international crisis (1975,1982 and 1991). However, these important analyses are only a dead letter if they do not impact on the design of the Fund's lending programs and if they do not end-up in clear policy messages to the membership.

In a similar way, Chapter 3 of the WEO, particularly BOX 3.1 (Does Inflation Targeting Still Make Sense with a Flatter Phillips Curve?), has a very important policy message that could be further developed and more clearly conveyed to the membership. In fact, the WEO is casting serious doubts on the benefits of one of the cornerstones of so-called mainstream macroeconomics: inflation-targeting frameworks. Indeed, the IMF staff states that "there are suggestions that, particularly in the current economic circumstances, inflation-targeting frameworks may be less than optimal". This is not a trivial matter and one that deserves the IMF's upmost attention, since it goes counter to 15 years of IMF policy advice to Latin America and other developing regions.

In the case of EMDCs, the Fund should assist monitoring and developing policies to control volatile short-term capital flows to limit financial risks and the appropriate use of macroprudential policies.

The Fund should rethink the recommendation of "preventive" recalibration policies to guard against the "eventual policy tightening in advanced economies", so countries are not in a position to adjust in a pro-cyclical way in case of a recessive scenario. This recommendation, in specific circumstances, could be considered correct if it refers to an individual country. Applying this advice to all EMDCs could result exactly in what is trying to be avoided; a fall of growth in these countries with its consequent impact in weakening the recovery process. In this vein, the Fund should not take on cyclical movements to impose structural reforms.

The Fund and other international organizations should continue working to support EMDCs to get long-term investment finance for infrastructure projects. Work undertaken by the G24, GGGI (Global Green Growth Institute) and LSE (London School of Economics) has estimated that infrastructure spending in the developing world will need to rise from its present level of around US$ 800 billion annually to around US$ 2 trillion annually in the coming decades.

Regarding LICs, it was a setback for these countries that the IMF reduced the access to Fund facilities for concessional financing by half. Notwithstanding, efforts to establish a self-sustained Poverty Reduction and Growth Trust (PRGT) should continue. At the same time, the Fund should advance on its agenda to deal with small, low-income states.

The Fund is pressing EMDCs and LICs to focus the subsidies on better targeting the beneficiaries. As a matter of fact, the huge subsidies in many sectors in AEs are never mentioned in IMF analyses and advice to these countries. In the case of energy, subsidies in AEs account for 40 percent of world subsidies, not to mention subsidies to agriculture production.

The Fund should support financing MENA countries when required.

III. Restoring Resilience

Collective action, with differentiated degrees of commitment and responsibilities, is required in specific areas to restore the world economy resilience. AEs should take clear steps to face the uncertainty that is constraining growth and impeding restoring resilience to the world economic and financial system.

Financial System Reform

Advanced countries need to commit to the reforms to limit uncertainty, arbitrage, and financial fragmentation. The Financial Stability Board (FSB) has addressed surcharges to global systemically important financial institutions (G-SIFI) and published the list of them. Pending priority issues are related to "too big to fail" problems, reforming over-the-counter derivatives trading, dealing with derivatives trading in commodities, agreeing on consistent accounting standards and dealing with shadow banking regulations and fiscal paradises and tax havens. The Fund should advance with the FSB on these issues and analyze and closely monitor financial stability risks that could emerge from continued monetary easing in key AEs.

High Deficit and Debt

Many AEs have improved their fiscal performance bringing neither growth nor debt reduction, but it is an important step forward creating more space to face them. Although it is true that in many AEs the debt levels relation to GDP are as high as those from the WWII era, and that several countries face large liabilities due to their support to the private financial system, it is also true that in recent decades several AEs already managed to deal with very high debts with no apparent problems. Low interest rates are expected to be maintained until 2015 and in the case of the post-war debt problems, they were solved through steady and continued growth. Thus, we can say that growth is all that is needed. Debt reduction through fiscal consolidation will reduce growth and in turn increase the relation of debt-to-GDP instead of reducing it.

In the euro area, despite the many policy steps taken, policy implementation remains insufficient to achieve the strong and balanced growth needed to secure debt sustainability and facilitate rebalancing within the monetary union. Something different should be done and where debt is unsustainable, ways to reduce the debt burden, such as debt restructuring, should be considered.

The Fund advises on the other hand, ambitious medium-term fiscal consolidation plans through subsidy and tax subsidy reform, broadening the tax base, instead of combating evasion and tax avoidance, the fiscal paradises, or encouraging taxing the financial system or the highest income recipients, and entitlement reforms which mean different ways of reducing pensions and health care funds.

Jobs and Inclusive Growth

We agree with the GPA that job creation and inclusive growth are imperatives that resonate in the entire membership. We support the Fund’s intentions to deal with growth and jobs, but we doubt the IMF’s capacity to deal with them in an appropriate manner. The Fund has more experience with policies that reduce growth and increase unemployment and the advice on Articles IV Consultations is along this line. In this regard, the Fund should review the experience of those countries that create jobs and inclusive growth to replicate the lessons of their experience.

Furthermore, the Fund’s approach to labor market flexibility and structural reforms related to the labor market, public employment, minimum wages, wages as an adjustment variable, productivity and the ignorance of labor migrations, should be reviewed. We support a deeper analysis, in collaboration with other relevant institutions, such as the International Labour Organization, of the growth and employment consequences of policy actions, tending to robust job creation and equity in income distribution. Staff’s directions toward a different approach to jobs and inclusive growth should be established.

In EMDCs, including LICs, policies to encourage productivity-led growth are critical in order for countries to reach their development aspirations and quality job-creation needs. In this regard, knowledge transfer and learning could drive the growth productive potential.

Global Imbalances and Spillover

Although since 2007 global imbalances have continued narrowing, the way in which this adjustment takes place raises new concerns. When surplus economies reduce their excesses and deficit countries diminish them, in the middle there are many countries that could be affected by an unarticulated process of narrowing imbalances which could lower global aggregate demand and/or modify the international trade structure.

The fall of trade demand from AEs to EMDCs should be replaced with domestic and regional demand and regional and south-south financial, trade, technological, and complementation agreements should be promoted and established. Today, several of these agreements already exist, such as utilizing domestic currencies in trade or developing joint equipment, machinery and industrial products or creating new regional or supranational bank institutions.

The impact of AEs' negative effects of accommodative monetary policies on EMDCs through side effects in capital flows and exchange rates impact on high asset prices and leads to the misallocation of resources in recipient countries. The IMF is launching several reports to highlight the consequences of unconventional monetary policies from different angles; the Spillover Report analyzes not only spillovers but cross border impact of policies' design to reestablish growth; the External Sector Report focuses on capital flows and the external balance assessment; and the Integrated Surveillance Decision deals with interconnectedness and spillovers in bilateral consultations. We hope that this battery of analysis supported by the global risk assessment matrices (G-RAM) will allow the Fund to fill the gap that led to the global financial crisis and will play its role in the surveillance of advanced economies.

IV. Adapting to the Future

In adapting to the future, the governance of the institution should be placed as the first issue on the GPA in order to enhance the Fund's legitimacy and effectiveness while strengthening the multilateral and cooperative nature of the Fund. The 2010 reform package, once adopted, will represent the pre-crisis world economic situation (the data used was up until 2008), that is, the global situation five years ago. It shows how the governance of the institution represents the appropriate and present views of the whole membership, particularly of EMDCs and LICs. Moreover, if the continued reform of the quota and governance structure is key to the Fund's legitimacy and effectiveness, the stagnant process for the 15th General Review of Quotas puts forward the deepened democratic deficit of the institution and the need for a profound transformation of the Fund.

The unforeseen case of Cyprus indicates, once more, that the role of the Fund in the run up to the financial and economic crisis should be revisited. In this regard, further progress should be made to promote the diversity of staff, particularly in regard to academic backgrounds, approaches and experiences. While the second external evaluation of the Independent Evaluation Office highlighted the need to review the board-management-staff interrelation and although the recommendations of the Ocampo Report were strongly endorsed, we are skeptical of their future implementation.

We agree with the GPA that the growing clout of emerging market economies is setting the stage for an increasingly multi-polar world where long-term trends shape the scenery of the global economy. It will depend on the Fund's openness to change whether this multi-polar world will be expressed inside or outside the institution.

Argentina

A decade of sustained and inclusive growth

Argentina and the region were witness to several lost decades. In contrast, the 2003-2012 period of sustained and inclusive growth can be considered a won decade for our country. Free from conditionalities, the Argentine economy initiated a significant structural transformation. Between 2003 and 2012, GDP doubled, with an average annual economic growth rate close to 7.2 percent, which constitutes the highest average growth rate in the country's economic history for such a long period. More importantly, this unparalleled economic growth has been socially inclusive, reflected in a clear reduction in poverty, unemployment, and inequality, making Argentina's GDP PPP per capita one of the highest in Latin America. While the IMF is now discussing Jobs and Inclusive Growth, Argentina has applied a policy towards these goals since 2003.

Despite the economic uncertainties in Europe and other AEs and their impact on the country, Argentina's economic resilience is due to a resonant macroeconomic framework. The main pillars are a strong domestic consumption tied to the increase in employment and standards of living, together with solid external and fiscal results, maintaining external public debt at a low and sustainable level, a managed floating exchange rate regime, the implementation of a macroprudential policy framework to face volatile capital flows, and the accumulation of foreign reserves, among other countercyclical policies.

After 9.2 percent growth in 2010, and 8.9 percent growth in 2011, during 2012 the economy grew by 1.9 percent in a context of economic turmoil in AEs, the fall of growth in Brazil and a persistent drought that impacted heavily on agricultural output. In 2012, exports fell by 3.3 percent with regards to 2011, particularly to Europe by -17 percent, the USA, -5 percent, and exports to the Northwest of Africa and Egypt, regions that in 2011 had received a similar amount of Argentinean exports as the USA did, fell by -19.6 percent. Although the Argentinean government managed to reverse the declining trend in production by the largest oil producer in the country, energy imports continue to drive the fall in the external surplus. Despite these challenges, the current account remained slightly positive. Industrial manufactures are the largest export item with 37 percent of total exports, followed by manufactures of agricultural origin with 32 percent and in third place, the exports of commodities account for 24 percent of total exports.

We strongly believe that equality is an important ingredient in promoting and sustaining growth. Since 2003, key components of the growth model are the creation of quality jobs, the progressive reduction of inequality, social inclusion and income distribution. During this period, 64 percent of new firms were set up; that is, almost 200,000 firms in industry, commerce and other services. Around 500,000 new jobs were created each year, and unemployment thus was reduced by 67 percent, decreasing from 18 percent in 2Q 2002 to 6.9 percent in 4Q 2012, with a strong increase in employment formalization. The number of workers with a formal job and social security contributions grew by 92 percent during this ten-year period. The minimum wage grew to be the largest in Latin America. In turn, the average real wage increased by more than 37 percent. The end-result was a historic increase in living standards, which is reflected in the doubling of the middle-class between 2003 and 2009, as found by a recent World Bank paper.[3]

Perhaps the most important measures were to enhance Argentina's social safety net which is based on several programs: the Universal Child Allowance Program "Asignación Universal por Hijo" provides coverage for more than 1,700,000 families and 3.3 million vulnerable children; "Argentina Trabaja", provides social inclusion through work and within this the program "Ellas Hacen" is oriented to women; "Manos a la Obra", initiates productive projects for families and self-employees; the Food Security Plan (Seguridad Alimentaria) has improved the subsistence capacity of more than 1,500,000 families; the program Actions for Social Promotion and Protection and the Plan for Pension Inclusion, among others. Two major initiatives deal with housing construction and renewal, Plan Federal de Viviendas, which has already achieved almost one million houses built, and PROCREAR, an innovative program to finance the construction and renewal of houses, which plans to finance 400,000 new houses in four years. These plans allowed for the reduction of poverty and extreme poverty. In 2003, the country recorded a poverty rate of 54 percent, of which 27.7 percent were in extreme poverty. Comparatively, at the end of 2012, only 6.5 percent of the population lived in poverty and 1.7 percent were classed as extremely poor. To deal with this hard core of poverty, the Plan Ahí has outreached 1,000 neighborhoods around the country and has served more than one million people.

Also, the social security system has increased its coverage from 3,158,000 beneficiaries in 2003, that is 66 percent of pensioners, to almost 6 million beneficiaries, reaching 94.3 percent of the elderly. These beneficiaries of the system of social security have a legal right, beyond the will of the government authorities, to an increase in their pension twice a year, based on a formula that guarantees pensions' purchasing power. Social spending on non-contributory pensions has also been increased. Expenditure on education has risen to 6 percent of GDP, in line with the Education Law. Argentina's Connect Equality Program (Conectar Igualdad), launched by Cristina Fernández de Kirchner to distribute approximately 3.5 million laptops to secondary school students, is being implemented successfully and 74 percent of the laptops have already been delivered. Finally, health spending has also been raised to prevent pandemics like the H1N1A flu and other diseases, such as dengue fever.

The government has focused not only on increasing the domestic demand but on enhancing income distribution. The recent implementation of a program for the rationalization of subsidies based on an income and wealth criteria, will allow the government to assign social spending more equally, guaranteeing the protection of the most vulnerable sectors of its population. As a source of social inequality, volatility in commodity prices is a menace against which Argentina has been historically vulnerable. Agricultural commodities play a very important role in the Argentine economy, as the country is a major producer, consumer and exporter of these products. In order to protect rural families, the government implemented specific programs of rural investment in order to provide thousands of families with technical assistance and financial aid, plus enlarge the rural electrical supply system, develop the irrigation system and open and improve kilometers of rural roads in order to improve productivity and increase the sown area of the agricultural sector.

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[3] Ferreira, Francisco H. G., Julian Messina, Jamele Rigolini, Luis-Felipe López-Calva, Maria Ana Lugo, and Renos Vakis. 2013. *Economic Mobility and the Rise of the Latin American Middle Class.* Washington, DC: World Bank.

After almost collapsing in 2001-2002, the financial system is now solvent, liquid, well-regulated and capitalized, thus allowing our economy to recover from the impact of the international financial crisis faster than others. It is resilient and effectively supervised, has large capital and liquidity buffers and the quality of their assets is strong. At the same time, the management of the impact of the global financial crisis was very appropriate. Liquidity and solvency levels remain high, in a context of reduced credit risk which is reflected in low levels of loan irregularity with respect to other emerging and developed economies. Favorable prospects for economic growth help to strengthen the conditions for financial stability. Return on Assets (ROA) and Return on Equity (ROE) that were negative in 2003 (-2.9 percent and -22.7 respectively) have been positive since 2005, and in November 2012 were 3.02 percent and 28.77 percent respectively. The Central Bank of the Argentine Republic has a new charter, approved by law in 2012, which broadened its objectives to adapt to the new stage. These include the pursuit of monetary stability, financial stability, employment, and economic development with social inclusion.

On the real side, investment grew by a significant 15 percent in 2010, and by 13.5 percent in real terms in 2011, accounting for 24.5 percent of GDP; a performance explained by both private and public investment. Although investment in 2012 fell by -4.9 percent to 22.8 percent of GDP, this figure is nevertheless well above the historical average. Long-term challenges are being addressed through the record rate of investments over the past 50 years and by doubling the percentage of expenditures in science and technology in relation to GDP, including thousands of fellowships per year for doctorate students. In 2007, the Ministry of Science, Technology and Productive Innovation was created to incorporate the benefits of science and technology and improve economic and social development. Investments in the provinces are supported by the government-established Federal Solidarity Fund (Fondo Federal Solidario), funded by a 30 percent export tax collection on soy complex, which has been oriented to infrastructure, such as building schools, houses, drinking water processing plants, and water and sewage networks.

The government has also implemented a range of policies to support the development of long-term finance for productive investments, particularly infrastructure and small and medium-sized enterprises (SMEs). These programs include, among others, the Bicentennial Program to Finance Production (Programa de Financiamiento Productivo del Bicentenario), the Productive Recovery Program (Programa de Recuperación Productiva), the so-called Inciso K whereby insurance companies provide funding to productive projects, and the active role of the FGS (Sustainability Guarantee Fund) is a provider of long-term finance and a lending program to renew the truckloads' fleet. In turn, micro-enterprises have received more than 320,000 micro credits. The Plan for Industrial Development 2020 to foster technological development in the industrial sector is being implemented, along with a new Strategic Plan Agri-food and Agro-industrial (PEA), which aims to increase grain production by 50 percent by the year 2020.

Since 2003, after the country's worst financial crisis that led to the default, Argentina applied a set of measures aimed at progressively normalizing public debt and creating a sustainable repayment capacity. These measures involved a successful debt restructuring process that reached a substantial level of acceptance—more than 91 percent of the eligible debt—was tendered to the two-phase exchange process that had taken place in 2005 and 2010. Over the past nine years, the debt-to-GDP ratio has been reduced from 166 percent to around 41.5 percent. The current public debt stock shows a balanced composition in terms of currency, duration, interest rates and types of creditors. In terms of debt with the private sector in foreign currency, the debt-to-GDP ratio came to less than 9.4 percent as of June 2012.

At the same time, Argentina is facing an extraordinary challenge dealing with creditors known as vulture funds, who seek privileged treatment through litigations within legal gaps even though they have acquired sovereign debt at cents on the dollar. Due to the lack of an international legal framework for sovereign debt restructuring, Argentina continues to deal with a minority of litigious creditors that impede a full completion of the debt-restructuring process. The country has presented all documentation required by judges in New York to deal with the requirement to propose an alternative payment to these vulture funds.

The debt normalization process, as well as the current policy of Argentina based on the goal of a strong debt reduction, is a positive signal giving the markets confidence in the country's ability to continue servicing its public debt on regular basis, despite the strong attack of hold-out creditors. In the same vein, it is well known that credit rating agencies do not reflect debtor solvency correctly; and in our case, current credit ratings do not reflect this effort from our country. Argentina is conducting a substantial reform of its CRA (Credit Rating Agencies) regulation that builds on international best practices and country experiences. However, it is necessary to continue discussing the role of credit rating agencies in international fora, particularly the G20, to propose concrete policies aimed at reducing dependence, enhancing supervision and increasing competition.

Argentina continues to advance step by step in strengthening its relations with the IMF. Argentina has demonstrated its commitment on working together on the bilateral agenda. The IMF has indeed made important mistakes in dealing with Argentina, as has been recognized by several former management and staff members of the Institution. Among others, Michel Camdessus, Raghuram Rajan and Agustin Carstens, have expressed their disappointment on how the IMF dealt with the currency board, the crisis and the decision not to participate in advising Argentina on the rescheduling of the debt. More recently, the relation with the IMF involves ongoing technical assistance to develop a new CPI on a national basis, the ROSCs that has been completed and published and, the FSAP report, which is underway after a joint mission to Argentina by the World Bank and IMF staff in March 2013.

A lesson has been learnt the hard way throughout Argentinean history: the crucial role that the State must play to achieve a steady, sustainable and inclusive path of economic development. Indeed, Argentina has strengthened its policy framework built upon a broad-based productive and socially inclusive development, a strong domestic demand, a balanced fiscal policy, a solid banking system, a sustainable debt, the accumulation of international reserves and the promotion of regional integration and international cooperation. Growth has been sustained and social indicators have improved considerably. Due to the structural transformation of the economy since 2003, Argentina is now well placed to address the challenges of an uncertain world economy. The government has put the country back on track and has restored its potential for economic, human, and social development. Strengthening and continuing with these outcomes will be the main objective for the future.

Bolivia

Economic performance has continued to be positive during 2012. In fact, the GDP growth rate has been 5.1 percent, keeping up with the dynamism reinstated in 2010, which stems from the impulse of exports, as well as domestic demand. The main drivers of growth were financial services and hydrocarbons. The trend of the latter is a result of greater exports and a buoyant domestic market for refined hydrocarbons. For 2013, the authorities are projecting a growth rate of 5.5 percent as public investment will likely be higher than in 2012, while inflation is projected to be around 4.5 percent.

The balance of payments has also attained positive results. The current account registered a surplus of 7.8 percent of GDP, a much greater level than in 2011, due to a strong trade balance, as well as greater remittances and direct foreign investment. Consequently, international reserves continue to grow providing a solid base to support a stable exchange rate, which also helps to anchor inflationary expectations—in a context of strong volatility and changing trends of exchange rate parities in neighboring countries—providing an environment of greater certainty and contributing to the process of *Bolivianization* (de-dollarization). At the end of 2012 international reserves were at $14 billion, representing more than 50 percent of GDP. External public debt is evolving smoothly and it is below 15 percent of GDP, while the total public debt (internal and external) is around 31 percent of GDP, showing a descending trend onwards. This trend gives the country room for borrowing if necessary. In October 2012, after 90 years, Bolivia successfully returned to the international financial markets issuing $500 million of ten-year sovereign bonds at a yield of 4.875 percent, which signals the strength of the fiscal and external accounts.

The conduct of monetary policy is carefully geared towards preserving adequate liquidity conditions and monitoring inflation developments, **while supporting growth**. Inflation by the end of 2012 reached 4.5 percent, very much in line with what the authorities expected. The authorities are remaining vigilant of the trend in prices and credit; thus in 2012, the monetary authority compensated the contraction in liquidity due to public deposits accumulation by gradually reducing the supply of monetary policy securities. Gradual reductions of securities of monetary regulation supply—accompanied by decreases in interest rates—were applied until reaching net redemptions in the third and fourth quarters. This policy and the increased deposits from the public favored the dynamism of the financial system which substantially increased its loan portfolio. The de-dollarization process continued its momentum due to inflation being under control, the bank reserve requirements policy, and the stability of the exchange rate. The real exchange rate is in line with its fundamentals—as intended by the authorities—to support the competitiveness of the economy. The financial sector stability has improved as it is growing steadily; nonperforming loans have reduced, provisions have increased, and profitability has also improved.

Fiscal accounts in 2012 showed a surplus following a tendency initiated in 2006. The fiscal authorities managed to reach surpluses in the last seven years, which allows fiscal room to overcome the effects from possible global slowdowns. As of December 2012, the fiscal position reached a surplus of 1.8 percent, while in 2011 the surplus reached 0.8 percent; even though the authorities are engaged in expanding public investment and had initially projected a manageable deficit. Bolivia will continue to follow its model for state-led economic development relying on a significant expansion of public investment, while at the same time aiming to reach fiscal discipline and sustained growth, with more equal income distribution through social programs to reduce poverty. Until the end of 2012, the combined public investment was around 11.5 percent of GDP. The fiscal authorities are seeking a greater efficiency in public finances administration, as well as expanding the tax base through administrative measures rather than tax increases.

Investments in oil and mining sectors are expected to increase from 2013 because the government has reached agreements in negotiating contracts with foreign companies, which—along with higher export—will permit to sustain government income to re-direct them to expand expenses for health, education, and infrastructure.

The authorities are doing their utmost to put in place a framework for the exploitation of their natural resources, allowing room for private investment, both foreign and domestic. The authorities' ultimate goal is to arrive at a framework that promotes the development of all natural resources sectors, with the proper checks and balances in place to ensure a fair share of the benefits for the Bolivian people. In the mining sector, it is necessary to revise the operating framework that allows a sustainable development over the medium and long term for both private and public enterprises. Development of the hydrocarbons and mining sectors are still key factors to Bolivia's future and to attaining a sustainable reduction in poverty levels.

Progress in reducing poverty has accelerated notably, in fact, extreme poverty has decreased from 38 percent in 2006 to 24 percent in 2012, but much remains to be done. In this regard, revenue re-distribution is an ongoing policy which is being pursued by fair adjustments in remuneration to the working people, as well as by conditional and non-conditional cash transfers, mostly to low-income families.

Chile

The **Chilean** economy has continued to expand steadily. Thus, in the period 2010-2012, GDP growth averaged 5.8 percent, without signs of macroeconomic imbalances, while achieving a pick-up in productivity growth. More recently, whereas the downside scenarios for the global economy have become less prominent,—thanks to the fledgling economy recovery in the U.S., steady growth in emerging Asia, and a calmer financial environment in the euro zone—domestic concerns have increased in importance. Growth in 2012 exceeded expectations, reaching 5.6 percent on the dynamism of investment and consumption. Large investment projects in mining and energy have sustained the pickup in capital formation, while full employment and rising incomes have buttressed private consumption. Despite the lack of slack in the domestic economy, inflation has remained subdued, and is currently running below the Central Bank's inflation target range of 2-4 percent.

In this context, the authorities have maintained a policy stance that reflects their vigilance towards potential risks. Despite low headline and core inflation, the monetary policy rate has been kept steady at 5 percent. A looser stance would not be appropriate given the strength of economic activity and domestic demand, and would incubate risks to medium-term inflation prospects and financial imbalances. Conversely, a tighter stance would exacerbate foreign exchange tensions in a context of persistently low global interest rates, a widening current account deficit and inflation expectations aligned with the target. Moreover, credit growth has remained moderate, and there are no obvious signs of financial overstretch. On the fiscal policy side, the central government exceeded its fiscal targets, achieving a lower-than-expected structural deficit in 2012 of 0.6 percent of GDP, consistent for the second consecutive year with an overall budget surplus, of 0.6 percent of GDP. For 2013, the authorities remain committed to achieving a structural deficit of 1 percent, aligned with the fiscal target laid out at the beginning of the current administration and the reconstruction efforts after the 2010 earthquake and tsunami.

After a number of years when the economy displayed significant current account surpluses, the balance of payments has shifted to show current account deficits, which is expected to reach 4.4 percent of GDP in 2013. The authorities see the move from a surplus to a deficit as the response of investment and savings to an environment of high terms of trade—in particular copper prices—which has proven more persistent than initially expected. Hence, mining companies have ramped up large investment projects, whereas the fiscal rule has gradually incorporated a higher medium-term price of copper for setting fiscal expenditures.

The widening of the current account deficit, coupled with Chile's high comparative economic growth, has been accompanied by an appreciation of the real exchange rate, which is now perceived to be on the strong side of the range consistent with medium-term fundamentals. Although the appreciating pressures pose a challenge for the conduct of policies, the authorities perceive that the flexible exchange rate regime, within an inflation-targeting framework, a fiscal rule, and a sound financial regulatory system, has served the economy well. Alternative policies within this framework, such as foreign exchange interventions, could be deployed in case of extraordinary circumstances, and in ways consistent with the flexible exchange rate regime.

A gradual deceleration of activity and demand is expected for 2013 and 2014 as the economy returns to trend. Going forward, the Chilean authorities will continue to closely monitor both domestic and external risks so as to implement the policies required to secure the macroeconomic and financial stability of the economy.

Paraguay

Paraguay continues moving towards a solid growth path in an environment of relatively low inflation and unemployment. This is the result of continued strengthening of the institutional framework and prudent implementation of fiscal and monetary policies; although at the end of 2012, the economy decreased by 1.2 percent, due principally to a severe drought and eruption of foot and mouth disease. However, non-agricultural GDP expanded at a rate of 5 percent, on the back of important fiscal impulse. There are strong indications that 2013 will rebound to a solid 10.5 percent growth, according to conservator predictions. The last quarter of 2012 already showed some improvement in the economy indicators.

Since mid-2012, the Central Bank of Paraguay (CBP) has maintained the profile of its monetary policy on a neutral stance. In this regard, the CBP monetary policy rate has remained at 5.5 percent. Annual inflation, as measured by the Consumer Price Index, closed at 4 percent by December 2012, below the target rate of 5 percent. Inflation remained subdued during the first quarter of the year and stood at 1.2 percent y-o-y in March 2013. The forecast for end-2013 is projected at 5 percent.

Imports of goods and services decrease by 5.2 percent by end-December 2012, explained by a decrease in goods. Exports also decreased 5.3 percent compared to the same period in 2012, mainly as a result of a decrease in goods, caused by the drought of the end of 2001. Currently the level of Net International Reserves is about 19.5 percent of GDP, providing enough buffers to deal with possible occurrence of external and internal shocks. The Real Effective Exchange Rate appreciated 10 percent in 2012 compared to its long-term equilibrium level. However, in 2013, there is an important recovery of the external trade. At the first quarter, goods and services exports increased 36.7 percent and imports by 12.9 percent.

Although annual credit growth in the financial sector has been relatively high in the recent past, during the first quarter of 2013 it shows a lower dynamic trend (14.2 percent), aligned to a sustainable long-run trend. Other indicators of the financial system remain sound and robust. Banks have strong capital and buffers, and low non-performing loans, despite last year's contraction of the agriculture and expected spillovers on the financial sector, which did not materialize.

Paraguay achieved several structural reforms during 2012. The country completed its action plan requested by FATF-GAFI, and GAFISUD to improve its AML/CFT regime and was removed from the gray list by FATF-GAFI. The government will approve its first National Strategic Plan on AML/CFT incorporating the most recent recommendations and best practices in the first half of 2013. The Personal Income Tax Law, which was postponed for many years, came into effect in August 2012, completing a comprehensive tax reform that began nearly a decade ago. The Central Bank and the Ministry of Finance completed the recapitalization of the Central Bank for an amount equivalent to about 3 percent of GDP, improving the financial position of the Central Bank. A Law named FONACIDE was enacted, locking in additional revenues worth US$ 300 million from Itaipu Hydroelectric Plant to be invested in infrastructure projects, education, health and long term financing. In January 2013, Paraguay issued its first international bond at the lowest rate for an inaugural bond in Latin American history, reflecting Paraguay's good macroeconomic performance over the last decade and the market's confidence on its growth potential over the medium term.

The initial forecast for 2013 indicates a strong rebound of at least by 10.5 percent, based on the recovery of agricultural production, the reopening of some markets to meat exports, and increased public and private investment. The government has recently sent to Congress a draft law for public-private partnership (PPP). Once approved, this law will provide the legal framework for the private sector to participate in large scale infrastructure projects.

Peru

Peru's economic growth is stabilizing around its long-term level. The economy expanded 6.3 percent in 2012, driven by the momentum of domestic demand, especially private and public investment. Consumer optimism has also been preserved and the markets show continuing confidence in Peru's solid growth, sound fiscal performance, sustained improvement of debt management, and lower exposure to foreign currency-denominated debt. At the same time, lingering global risks (debt crisis in Europe, slow U.S. growth, and moderate recovery in China) continued to weigh on the performance of emerging market economies in 2012.

The current account deficit increased to 3.6 percent of GDP in 2012 due to deteriorating terms of exchange and growing imports associated with high domestic demand and mining projects. On the fiscal front, while expenditure implementation accelerated (especially public investment), higher revenues raised the public sector surplus to 2.1 percent of GDP, higher than in 2011 (1.9 percent of GDP). The government remains committed to enhancing the quality and coverage of social programs.

Twelve-month inflation decreased in line with expectations, from 2.65 percent in December 2012 to 2.45 percent in February 2013 (within the 2 percent ± 1 percent target band), reflecting the reversal of supply-side factors affecting food prices and the central bank's prudent monetary stance.

In a volatile global context, the authorities are committed to preserving financial stability. In this regard, their attention has turned to establishing a set of macroprudential policies to limit systemic risks; and the central bank stands ready to use its considerable reserve buffer in case of sudden capital reversals.

Uruguay

Remarkable Performance…

Amidst a thorny global scenario, 2012 constituted another year of noteworthy economic and social developments in Uruguay. Once again, the country exhibited a GDP growth above the average of the region and a much higher rate compared with its two neighbors, Brazil and Argentina. For a long time, Uruguay's economic growth followed those of the above-referred countries very closely. How has this strong delink been possible? Among other factors, it is possible to cite Uruguay's decisive strategy to diversify products and markets along with a sizeable boost of investment, which clearly mirrors Uruguay's sound economic policies and a number of structural changes that have characterized the ongoing transformation process. Meanwhile, the substantial drop in unemployment and the rise in the population's income as well as social policies have allowed Uruguay to display critical progress in social conditions: the percentage of people under the poverty line is currently 12.4 percent (34.4 percent in 2006) and under extreme poverty is 0.5 percent (2.7 percent in 2006); moreover, income distribution has systematically improved in the last years (for instance, the Gini Index has varied from 0.44 in 2009 to 0.38 in 2012). Economic and social developments do not follow separate paths. A comprehensive concept of stability—including economic, political and social stability—is clearly enrooted in Uruguayan society and reflected in the authorities' objectives and instruments.

…but not exempt of substantial challenges and risks

Of course, the global economic situation—plentiful of substantial uncertainties—, many dimensions of regional circumstances, and certain domestic issues unavoidably bring about important challenges and risks to the country.

Eminently, developed countries have tried to tackle their challenges through "super-loose" monetary policies, ensuing strong appreciation pressures in many developing countries, including Uruguay; commodities prices have been exerting considerable inflationary pressures; abundant global liquidity along with Uruguay's strong performance, which leads to regaining the status of investment grade for the country, buttresses short-term capital inflows; unemployment rates, which are at historic low levels (currently at 6.1 percent), amidst a tight labor market (including a major challenge for the country with regard to a shortfall of skilled workers in some areas) have led to considerable wage increases—although, in recent years, they do not seem to reveal a relevant misalignment with regard to productivity variations; a severe drought in 2012 produced a significant fiscal burden, which reflects a much more widespread concern related to the country's infrastructure constraints; and substantial trade restrictions as well as a considerable economic deceleration have been observed at regional levels.

The Uruguayan authorities are well aware of these challenges and risks and have prepared appropriate responses to confront them; the build-up of substantial buffers points to a distinctive characteristic of the policies' design; of course, these buffers are not exempt of—important—costs, but the government believes that they are unavoidable to successfully face an uncertain global future.

How has Uruguay managed the above-referred complex constellation of global, regional and domestic factors?

From the monetary side, the central bank has responded to inflationary pressures with a monetary tightening which implied a cumulative increase of 300 basis points in the last two years, while raising average reserve requirement and introducing marginal requirements. Furthermore, after decades of bad experiences with rigid exchange rate schemes, Uruguay has decided to maintain a flexible system, which has served the country well as an important shock absorber. At the same time, as mentioned, "super-loose" monetary policies in developed countries, along with Uruguay's attractiveness for foreign capitals, has obligated the country's central bank to intervene in the exchange rate market in order to react against—a likely—transitory shock, thus, avoiding a misalignment of the exchange rate from its fundamentals. The latter has led to a reserve accumulation and a related sterilization response, which have involved a considerable cost for the country. Developed countries should be aware of the huge cost—in this case, in terms of quasi-fiscal deficit—that their policies have been instigating in many developing countries. In Uruguay's case—differently from some other countries—this cost is included in the country's fiscal figures, such as those presented in the IMF staff reports and in official statistics. Inflationary pressures and the considerable cost derived from exchange rate interventions constitute primary concerns for the authorities, and, as usual, they continue to evaluate ways to improve instruments and policy coordination. Of course, macro-prudential policies have occupied a relevant role in strengthening financial stability.

From the fiscal side, prudent policies remain in place following a consistent way of reinforcing fiscal sustainability and contributing to Uruguay's economic and social developments. It is worth underlining that the net public debt target was overreached in 2012; meanwhile, fiscal deficit in 2012 presented a considerable increase from previous years, which is, to a large extent, the consequence of temporary factors (such as the drought-induced cost of more than one percentage point of GDP) and the above-referred intervention in the exchange rate market.

Reaping the fruits of years of efforts and reforms: The illustrative cases of investment and the financial system

Over the last years, Uruguay has exhibited a notable raise in its investment rate, for instance from 14 percent of GDP in 2001 (close to the country's historic average) to 22 percent in 2012. As part of this process, it is relevant to underline the substantial arrival of foreign direct investment—being, at an average of 6 percent of GDP in the last eight years, one of the two countries in the region with the highest levels relative to their respective products. How has such a drastic change been possible? It is possible to cite many factors, but macroeconomic and financial stability, the country's traditional efforts to honoring commitments, transparent and appropriate incentives, the quality of institutions, as well as the investors' perception of promissory perspectives unambiguously constitute relevant explanation of this transformation.

Meanwhile, the drastic reforms of the Banco de la Republica Oriental del Uruguay (BROU), Banco Hipotecario del Uruguay (BHU) and the Superintendency of Financial Services, among other structural changes, are reflected in the financial system's sound indicators in terms of capital, liquidity and non-performing loans. Nonetheless, these indicators may not entirely cover other critical positive developments the system has displayed in the recent past, such as the substantial delink from non-resident, eminently from Argentina. In one decade, non-resident deposits in the country's financial system decreased from about 40 percent to somewhat above 10 percent, while credit to non residents declined from 20 percent to 0 percent.

Buffers to confront uncertainties

How will the day be after the "ultra-loose" monetary policies in developed countries? What will be the future of interest rates and the main global currencies? Do the current developments have a temporary or permanent nature? The strong uncertainty behind these and other aspects of the global economy led the Uruguayan authorities to the decision of building important buffers, being aware, meanwhile, that this entails present costs. Among others, it is possible to underscore: international reserves at 27 percent of GDP (almost depleted in 2002); average time to maturity of public debt at 11 years; public debt in domestic currency at 55 percent (almost negligible one decade ago); etc. Clearly, Uruguay's fiscal deficit could have been smaller in case this process of reducing risks had not materialized. However, Uruguay's economic and social situation and its outlook seem to have been rewarded from this approach.

Conclusion

Over the last decade, Uruguay has been systematically showing higher GDP than the region. Even more important, the country's economic growth has been broad-based (from the supply and demand point of view) and better distributed, making the process less vulnerable and more inclusive. Furthermore, Uruguay's potential growth has substantially increased. Eight years ago, the IMF estimated medium-term growth at 2 percent; currently, it is foreseen at 4 percent that is very close to the projected real GDP increase for 2013. The latter implies a clear deceleration from previous years (which would contribute to moderate inflationary pressures), but still a robust rate. As underscored, challenges and risks are considerable, but Uruguay's policies and reforms will continue to further reinforce the country's fundamentals and pave the way for further economic and social development.