

INTERNATIONAL MONETARY FUND

Statement by the Managing Director to the IMFC on the Fund's Lending Role and Surveillance Priorities

October 8, 2008

We are meeting in the midst of a financial crisis of historic proportion. Its broader effects on the global economy remain uncertain. But as the ripples are being felt across the world, we are reminded that globalization is not a slogan but a vivid interdependence. Dealing with the fallout of the current crisis is, of course, the immediate priority, alongside our on-going efforts to help our low-income members hard hit by the food and fuel price shock.

The Fund has a central role to play in helping members tackle this challenge, drawing on its experience in crisis management and its in-depth country knowledge. Fund staff has done extensive analysis of the crisis and its spillovers drawing on lessons from past crises, and disseminated information, analysis and policy advice through the Executive Board and intensive contacts with our members. We have also stepped up crisis preparedness efforts and are in close touch with individual members experiencing stress, standing ready to help with further advice and financial assistance. Meanwhile, we have been working intensively with the Financial Stability Forum on responses to the current crisis, which too will inform our discussions. But we should also look ahead and consider what this crisis implies for the Fund's financing, surveillance and collaboration roles, to help steer through the current turmoil and prevent future threats to global financial stability and prosperity. Let me set out for discussion some undertakings that will help the Fund rise to these challenges.

The IMF's Lending Role. We are of course ready to move quickly to provide financial support to our members at this time, using to the maximum the flexibility in our existing instruments and emergency procedures. It is particularly critical, however, that we have in place a robust lending function that meets our members' needs—whether financing, signaling or insurance. As the global financial system and members' needs have changed enormously since the Fund was created, the model for the present set of lending instruments may need to be adjusted to remain suitable for the needs of the overall membership. I have therefore launched a review of our lending role. Based on an initial discussion at the Board, we have developed a road map to advance work *concurrently* in five broad areas: (i) exploring analytical considerations for Fund lending; (ii) advancing the work on a new liquidity instrument; (iii) re-examining conditionality ; (iv) reviewing our lending role and facilities for low-income members; and (v) reviewing access limits and financing terms for using Fund resources. My plan is to have preliminary discussions with the Board in all these areas by the Spring Meetings, and to take decisions as quickly as possible in those areas where there is a strong consensus and particular urgency [(e.g., liquidity instrument)], with a view to reaching decisions before the 2009 Annual Meetings in remaining areas.

Surveillance Priorities. To help manage the current crisis and beyond, we must help members understand the interdependence of their economies and policy decisions, and promote collaboration or globally consistent actions. Doing so requires being more insightful, courageous, and persuasive. My vision for realizing this goal rests on four priority areas where I believe we can deliver unique value-added if we focus our efforts:

- ***Early warnings are needed to help keep policymakers ahead of events.*** To focus policy, the Fund should provide clear assessments of risks to baselines, including insights from global or regional risk analysis. To help do so, we are extending our periodic vulnerability diagnostics exercise to advanced economies and will strive for innovative ways of assessing and communicating risks, trying to be neither too coded nor too alarmist.
- ***Understanding macro-financial linkages is crucial.*** Recent surveillance has offered examples of high quality macro-financial analysis, and described key vulnerabilities and risks. But the current crisis shows that more is needed. We are intensifying work to guide everyday macro-financial analysis and update our toolkit for financial stability analysis, so that today's best practice becomes tomorrow's norm.
- ***Multilateral perspectives are integral to Fund surveillance.*** The current crisis is giving strong impetus to more thorough treatment of cross-country financial linkages. Staff will continue efforts to give more prominence to work on cross-country themes, and to better draw out the policy implications of multilateral surveillance findings.
- ***Exchange rates and external stability remain key focus areas.*** Our exchange rate assessments have improved, but they need to be cast in a broader external stability context—encompassing capital account developments and global foreign exchange markets—and integrated into the assessment of the overall policy mix. We are continuing to strengthen methodologies. Meanwhile, where there are significant concerns about external stability matters, I have proposed that we have closer engagement with members through *ad hoc* consultations.

These priorities are now encapsulated in the Fund's first *Statement of Surveillance Priorities* recently adopted by the Executive Board (attached). The Statement further identifies four key interlocking policy objectives : (i) resolve financial market distress; (ii) strengthen the global financial system; and (iii) adjust to sharp changes in commodity prices; and (iv) promote the orderly reduction of global imbalances. I hope you can endorse the thrust of this Statement, and reiterate members' willingness to work with the Fund toward these objectives, including by welcoming a financial diplomacy role for the Fund to gather a consensus on lessons and principles to underpin a stronger global financial architecture in the future.

SURVEILLANCE PRIORITIES FOR THE INTERNATIONAL MONETARY FUND, 2008-2011

In pursuit of its mandate to promote international monetary and financial stability, IMF surveillance will be guided through 2011 by the following priorities:

Economic priorities

The global economy faces a period of severe financial distress and slower growth alongside the challenges of sharp commodity price changes and global imbalances. The following interrelated policy objectives will be key to return to an international environment more conducive to sustainable noninflationary growth:

- **Resolve financial market distress.** Restore stability and minimize the adverse impact of the current crisis in financial markets on the real economy;
- **Strengthen the global financial system** by upgrading domestic and cross-border regulation and supervision, especially in major financial centers, and by avoiding the exposure of capital-importing countries, including low-income countries, to excessive risks;
- **Adjust to sharp changes in commodity prices.** React to commodity price shifts in domestically appropriate and globally consistent ways, with emphasis on keeping inflationary pressures in check in boom phases and minimizing risks that could arise when prices fall;
- **Promote the orderly reduction of global imbalances** while minimizing adverse real and financial repercussions.

*In coordination with other International Financial Institutions, the IMF should **promote a common understanding** of the forces and linkages underlying these challenges; **draw key lessons** from different experiences to share across the membership; **provide clear advance warnings of risks** to global economic and financial stability; and **advise on how best to use policy**—in particular monetary, fiscal, exchange rate, and financial sector policies—in support of these objectives.*

Operational priorities

- **Risk assessment.** Refine the tools necessary to provide clear early warnings to members. Thorough analysis of major risks to baseline projections (including, where appropriate, high-cost tail risks) and their policy implications should become more systematic;
- **Financial sector surveillance and real-financial linkages.** Improve analysis of financial stability, including diagnostic tools; deepen understanding of linkages, including between markets and institutions; and ensure adequate discussion in surveillance reports;
- **Multilateral perspective.** Bilateral surveillance to be informed systematically by analysis of inward spillovers; outward spillovers (where relevant); and cross-country knowledge (as useful); and,
- **Analysis of exchange rates and external stability risks.** In the context of strengthening external stability analysis, integrate clearer and more robust exchange rate analysis, underpinned by strengthened methodologies, into the assessment of the overall policy mix.

The Executive Board has set the above priorities to foster multilateral collaboration and guide IMF management and staff in the conduct of surveillance. These priorities look ahead three years, but may be revised if circumstances warrant. They will guide the Fund's work within the framework for surveillance provided by the Articles of Agreement and the relevant Board decisions, including the 2007 Decision on Bilateral Surveillance. Moreover, traditional areas of strength (such as fiscal policy and debt sustainability analysis) and relevant country-specific issues should not be overlooked.

The Executive Board is responsible for conducting, guiding and evaluating surveillance in order to ensure the achievement of these priorities. Management and staff are responsible for delivering on the operational priorities, subject to members' cooperation in line with commitments under the Articles of Agreement. To foster progress toward economic priorities, management and staff are responsible for providing candid high-quality analysis and effective communication. The Managing Director will report: (i) regularly on actions toward priorities and readily visible results; and (ii) at the time of the next Triennial Surveillance Review on progress in attaining these priorities; management's and staff's contributions; and factors that impeded progress.