



International Monetary and Financial Committee

Fourteenth Meeting
September 17, 2006

**Statement by Eero Heinäluoma
Minister of Finance, Finland**

On behalf of Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway,
Sweden

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Main messages

- *Global expansion is strong and broadly based, but the downside risks highlight the need for a renewed spirit of multilateralism.*
- *The new multilateral consultation procedure, a strengthened regional dimension, together with focused and streamlined bilateral surveillance should be important elements in enhancing the effectiveness of surveillance.*
- *We support the package of reforms on quotas and voice as laid out in the Resolution of the Board of Governors and await its prompt and full implementation. We urge all members to put a strong effort into reaching agreement on the issues to be resolved during the second stage. Throughout this work, simple and transparent principles as well as equal treatment of all member states remain vital.*
- *A reformed Fund should be efficient, flexible and responsive to Members' needs. It is important to ensure good governance, including transparent and legitimate decision-making, also within the Fund. All strategic policy decisions should be prepared and taken by the Executive Board.*
- *While the best prevention against crises is self-insurance through sound macroeconomic policies and supporting high quality institutions, we are open to discuss proposals for a new financing instrument to support crisis prevention.*
- *Paying particular attention to ensuring that debt remains sustainable, the Fund should assist low-income countries in areas within its core mandate and with a clear division of responsibilities between the various institutions.*

Introduction

1. A key aim of the Medium-Term Strategy (MTS) is to ensure that the Fund remains relevant for all of its Members. A reformed Fund will have to be efficient, flexible, responsive to Members' needs and equipped with appropriate governance structures. Progress in modernizing Fund governance has become crucial for the credibility of the Fund.
2. Global expansion is strong and broadly based, but the balance of risks is increasingly to the downside with emerging inflationary pressures, high oil prices, geopolitical tensions, growing protectionist pressures as well as the remaining possibility of a disorderly unwinding of the large global imbalances. We need a renewed spirit of multilateralism to achieve progress on many fronts, including to revive the WTO Doha negotiations and to make further progress towards the Millennium Development Goals. Everyone should stand ready to compromise in order to reach the common longer term goals that benefit all.

Enhancing the effectiveness of surveillance

3. In our view, enhancing the effectiveness and focus of surveillance is the most important element of the MTS. This will require a package of measures, some of which have already been brought to the Board for a first discussion. We welcome the new multilateral

consultation (MC) procedure that is designed to complement regular Article IV consultations. It could play an important role in promoting multilateral action and could also help to reinforce the Fund's role as the central forum for discussion on global issues. To ensure legitimacy, it is essential that the MC procedure is appropriately embedded in the Fund's governance structure and the involvement of the Board and the IMFC is guaranteed. The first MC on global imbalances should promote action to help unwind global imbalances in an orderly way.

4. Bilateral surveillance remains the core of Fund surveillance. Article IV consultations should be more selective and focus on the main macroeconomic and financial policy challenges to promote domestic dialogue on the longer-term policy issues. In this context, we see merit in the proposed streamlining of Article IV consultations. When appropriate 24-month cycles should also be considered for highly stable non-systemic countries. It is central that streamlining actually results in savings for the Fund.
5. The links between the different levels of surveillance should be further strengthened. Multilateral and regional surveillance will have to build on bilateral surveillance and the spillovers and other relevant issues identified in multilateral and regional contexts will have to feed appropriately back into bilateral surveillance.
6. It is important to fully integrate financial sector surveillance with general macroeconomic surveillance. The new Monetary and Capital Markets Department is well placed to take up this challenge. The Financial Sector Assessment Program should remain a key tool for financial sector surveillance and we encourage those systemic countries that remain to be assessed to participate at an early stage. The development of modalities for regional surveillance has moved forward in the area of financial sector surveillance. The ongoing regional financial sector surveillance project for the Nordic and Baltic countries is an example of such work and we believe that lessons can be drawn from both the analysis and the process for other regional surveillance projects as well.
7. We look forward to the more detailed proposals after the Annual Meetings regarding the Review of the 1977 Decision on Surveillance over Exchange Rate Policies. While the Decision should remain focused on exchange rate policy surveillance, the review should be used to clarify the place of exchange rate surveillance within the broader context of surveillance.
8. To consolidate the key objectives and priorities of the Fund's multi-layered surveillance framework in a single concise document, the Executive Board is considering setting a new remit for IMF surveillance. The IMFC could play a role in conferring political legitimacy and visibility on a remit. Considerable progress has recently been achieved in making the remit concept operational, but further clarification of its content, structure and relationship to other remit-like devices is needed to guarantee that it would truly strengthen the Fund's surveillance framework.

Governance

9. We support the package of reforms on quotas and voice as laid out in the Resolution of the Board of Governors. The initial ad hoc quota increase to a few underrepresented members and the increase in the staffing entitlement of the Executive Directors' offices of particularly large constituencies should be implemented promptly in order to demonstrate concrete progress in the wake of the Singapore Annual Meetings. However, more work needs to be done in line with the actions and timetables outlined in the Resolution. While not prejudging the outcome of the work on a new quota formula, we continue to emphasize that the distribution of quotas should adequately reflect the role of the Fund, thus due weight should be given to GDP and ability to contribute financially as well as openness of the economy. Furthermore, the voice of low-income countries should be further strengthened by, inter alia, at least a doubling of basic votes. We urge all members to put a strong effort into reaching

agreement on the issues to be resolved during the second stage. Throughout this work, simple and transparent principles as well as equal treatment of all member states remain vital. We must strive for clear rules that stand up on their own and do not need to be supported by a web of implicit agreements.

10. It is important to ensure good governance, including transparent and legitimate decision-making, also within the Fund. In order to respect the role of the Executive Board, all policy decisions must be prepared and taken by the Board. The IEO is well placed to provide an objective view on governance within the Fund and we look forward to its report on "Aspects of IMF Corporate Governance – Including the Role of the Board".
11. The proposals in the MTS for streamlining Fund documents and procedures are a move towards a reformed and more efficient Fund. The recent streamlining of the guidelines for misreporting is a welcome example of providing the Board and Management with more room to focus on strategic issues. It will be important for the Board to monitor that the momentum for progress in streamlining continues.

Fund finances

12. Ensuring sound Fund finances is a key element of the MTS. We welcome the two-pronged strategy agreed by the Executive Board to place the Fund's income position on a sustainable footing. The activation of the investment account marked a welcome, albeit still modest step in broadening and strengthening the income base. The continued, faster-than-anticipated decline in outstanding credit underscores the need to consider a full range of options, including using the investment revenue from a limited sale of gold, to ensure a sustainable income base for the Fund over the long term. We look forward to the upcoming report of the Committee of eminent persons that will be an important input to future Board deliberations on securing sound Fund finances.
13. The Board must also continue to explore further options to reduce the Fund's administrative expenditures especially in line with a reduced administrative burden from declining lending. In implementing the MTS it should be kept in mind that if proposals in some area increase costs, offsetting savings will have to be found somewhere else. We urge that the recently introduced medium-term budgeting framework is used to the greatest extent possible.

The Fund's role in emerging markets

14. The best prevention against crises in emerging markets, and more generally in all countries, is self-insurance through sound macroeconomic policies and supporting high quality institutions. Other types of insurance cannot replace this first line of defense. Countries should try to avoid balance sheet vulnerabilities and adhere to international best practices in the areas of transparency and financial sector standards and codes. The role of Fund surveillance is crucial in achieving and monitoring progress in these self-insurance areas. To get additional protection against shocks, a country may consider collective insurance arrangements such as regional or other pooling arrangements. In our view, the Fund should stand ready, if requested, to support such arrangements.
15. We recognize that there are developments that warrant further analysis of a new financing vehicle for crisis prevention. Accordingly, we are open to explore further the concept of contingent financing. The recent proposal, which outlined the main features of a Reserve Augmentation Line, provides a good starting point for further discussions. Considering the failure of the CCL, and given the difficult outstanding issues, the discussions must be frank, straight-forward and solution-oriented.

The Fund's role in low-income countries

16. The Fund plays an important role in low-income countries and should focus on macroeconomic issues and institutions relevant for macroeconomic and financial stability. The low-income countries themselves have the primary responsibility to put in place sound policies and strong institutions. This is essential for securing predictable and increased aid flows. The Fund should assist the countries by providing policy advice, technical assistance and financial support.
17. The division of responsibilities between the various institutions assisting the low-income countries needs to be clear and effective. Cooperation and coordination should be operative and efficient - fully utilizing respective comparative advantages. The External Review Committee on Bank/Fund collaboration should make concrete proposals for clarification of the respective responsibilities.
18. Assisting low-income countries in establishing and maintaining a policy environment conducive to sustainable economic development and sound institutions is clearly within the Fund's mandate. Close and clear dialogue with both the donor community and the recipient country is key. We welcome the Fund's engagement in assisting low income countries in managing aid flows. We see an important task for the Fund in providing advice to member countries on how to ensure that these aid flows support macroeconomic and financial stability on a viable basis. But the Fund should be careful in passing judgment on the aid flowing into these countries to avoid the risk of being perceived as an obstacle to aid and the achievement of the MDGs. It is outside the mandate of the Fund to assess what the financing needs are for achieving the multiple MDGs in each country.
19. We welcome the prompt implementation of the multilateral debt relief initiative (MDRI) on the Fund's part. Going forward, the Fund should continue to assist the countries that have received debt relief with a particular focus on ensuring that they do not rebuild unsustainable debt. A new lend- and forgive cycle must be avoided. Achieving and maintaining debt sustainability is a shared responsibility between debtors and creditors, including emerging market lenders. It is especially important to avoid non-concessional lending to countries with a recent history of unsustainable debt. The IFIs have a crucial monitoring role based on a strong and comprehensive debt sustainability framework. This framework should ensure that new borrowing is limited, undertaken at a measured pace, and has strong economic justification. It should also address incentives for borrowers and creditors to prevent moral hazard and free-rider problems. The Fund should assist the countries in implementing sound medium-term debt strategies and strong public expenditure management systems. Good governance - including fighting corruption - accountability and sound economic management are crucial.