

WORLD BANK GROUP

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Statement by the Hon. **HENRY M. PAULSON, JR.**,
Governor of the Bank and the Fund for the **UNITED STATES**,
at the Joint Annual Discussion

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Welcome to Washington. I'm pleased with the new leadership we have at the World Bank and the IMF. I have great confidence in Bob Zoellick and he has clearly hit the ground running. I am really looking forward to working with Dominique Strauss Kahn—a proven leader. And a big thank you to Rodrigo de Rato for his leadership over the last few years. I wish him the best in his future endeavors.

The Changing Global Economic and Financial Landscape

The context to these annual meetings is continued strong global economic conditions and the recent financial turbulence. This context reminds us of the changing and challenging financial landscape and how imperative it is that we adapt ourselves and our institutions to meet these challenges. Let me hit on a few of the key changes we see. First, deeper, more sophisticated, more globally-interconnected capital markets have helped underpin growth in both developed and developing countries, but have also created new complexities. Second, global growth and financial soundness depend increasingly on dynamic emerging market economies, rather than overwhelmingly on industrial countries. Finally, accelerating globalization has heightened our awareness of the links between energy and environmental policies and longer-term global economic prospects.

International capital markets have become more efficient and offer a growing array of innovative financial instruments. The volume of cross-border financial flows has expanded substantially in just the last five years, as has the daily volume of foreign exchange transactions. Innovation brings important economic benefits, promoting growth through the efficient allocation of capital, increasing access to credit and helping spread risks more broadly. But innovation has also brought increased complexity, new risks, new challenges and some new problems, which are now being examined by policymakers and regulators. We need to continue to be vigilant, because all of our capital markets are not yet functioning normally. As we move to address current problems, we must also address policy issues to prevent a repeat of recent excesses. Cooperative bodies like the Financial Stability Forum, the Basel Committee on Banking Supervision and the International Organization of Securities Commissions have a key role to play internationally, complementing domestic regulatory responses.

Global economic trends are increasingly impacted by developments in emerging markets. China, India and Russia presently account for half of global growth. Emerging markets as a whole are growing more than twice as fast as industrial economies, and account for a rising share of global trade and investment. Such realities need to be reflected in international financial and economic institutions, both in the focus of their work, and in their governance structures.

Any long-term view of global economic prospects must take into account energy security, deal with the global challenge of climate change and address environmental impacts for future generations. The cross-border nature of this challenge points to the need for international approaches. President Bush's major economies initiative, to work with the world's largest producers of greenhouse gas emissions to reach agreement by 2009, and his proposal for an international clean technology fund are important steps in this direction.

Modernizing the International Financial Institutions

To remain relevant in this changing landscape, the international financial institutions must better define their core missions, and align staff and other resources accordingly. Future credibility of the institutions also requires that governance structures evolve to reflect new global realities.

International Monetary Fund

A defining issue for the IMF is how to exercise effective surveillance over member country exchange rate policies in a world of fixed and flexible exchange rate regimes. The recent updating of the IMF's exchange rate surveillance mandate was an essential step, and implementation is equally critical. IMF staff needs to roll up their sleeves, undertake thorough analysis, and put forward their judgments. Without meaningful exchange rate surveillance, governance and management reform will ring hollow.

Fundamental changes to the IMF's governance structure to reflect the growing role of dynamic emerging markets in the global economy must remain a priority. While such changes are not easy to achieve, a strong, credible IMF is in all of our interests. On behalf of the U.S., it is time that we ask emerging markets to take on greater responsibility in the international financial system. But it is fair for them to ask for a greater share in representation in return.

Changes are also needed to put IMF finances on a sustainable footing. One part of the solution must be to reduce expenditures by re-evaluating the IMF's core mission and making difficult decisions on priorities. Hand-in-hand with this, we recognize that we need to consider longer term sources of income for the IMF over the next year.

Multilateral Development Banks

Multilateral development banks also must adapt while continuing to focus on their core missions of economic growth and poverty reduction. On the one hand, there is the challenge of their continuing relevance in countries whose economic success means they no longer need MDB finance. On the other, the poorest countries – especially in Africa – continue to need concessional assistance that is results-oriented, performance-based and focused on each bank’s comparative advantage. We look forward to a successful replenishment of IDA to help meet those needs.

Fighting corruption, a fundamental challenge to growth and development, must continue to be central to World Bank operations and policies, as the Volcker committee has recently reminded us. In addition, access to energy and the consequences of climate change have clear implications for growth in the developing world, and the World Bank can and must respond.

The World Bank must also enhance coordination among the World Bank Group itself to serve as one institution on behalf of its clients. At the same time, it must maintain a rigorous focus on defining, managing for, and achieving the desired results. Addressing these multifaceted challenges is no small task, but one that shareholders are demanding and deserve.

I look forward to working together to advance this important agenda.