

INTERNATIONAL MONETARY FUND

WORLD BANK GROUP

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL FINANCE CORPORATION
INTERNATIONAL DEVELOPMENT ASSOCIATION
INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES
MULTILATERAL INVESTMENT GUARANTEE AGENCY

J

Press Release No. 2

October 13, 2008

Address by **DOMINIQUE STRAUSS-KAHN**,
Chairman of the Executive Board and
Managing Director of the International Monetary Fund,
to the Board of Governors of the Fund,
at the Joint Annual Discussion

**Remarks by Dominique Strauss-Kahn, Chairman of the Executive Board and
Managing Director of the International Monetary Fund, to the Board of Governors of
the IMF at the Joint Annual Discussion, 2008 Annual Meetings of the International
Monetary Fund and the World Bank Group
Washington DC
October 13, 2008**

Mr. Chairman, Governors, honored guests, it is a pleasure to welcome you to these meetings on behalf of the International Monetary Fund.

We meet at a critical time. We are living through the most dangerous financial crisis since the one that led to the Great Depression. Many people have observed that some aspects of the current crisis are similar to that terrible crisis: among the public, over-optimism followed by a faltering of confidence, in the markets, mania followed by panic. Many people fear that the economic consequences could be as important.

I do not share this view. The world is a very different place now from the '30s. We have learned from the mistakes of the past, and we have learned from each other's experiences. We have tools to manage markets and economies now that we did not have then. We have the will to use them. I am confident that we can emerge from this crisis with our economies and our societies intact.

To succeed, we must do three things.

We must act quickly.

Between the stock market crash of 1929 and March 1933, when a new president took office, two-fifths of the banks in the United States were closed and unemployment rose to almost 25 percent. We cannot let this happen again. We cannot wait while banks fail and jobs are lost.

We have already acted quickly. Central banks have injected liquidity; governments have mobilized to arrange the orderly takeover of key financial institutions and to guarantee deposits. Emerging economies with ample reserves cushions have used them to provide foreign exchange to their banks as needed.

We must act comprehensively and imaginatively.

In the '30s countries acted in a piecemeal way, and were hamstrung by old-fashioned orthodoxies.

Instead, we are acting imaginatively. Governments have already been prepared to break with precedent and try new approaches. Increasingly, these approaches are comprehensive, attacking all aspects of financial market problems: liquidity, bad assets, shortage of capital, and especially confidence.

We must act cooperatively.

An upsurge of nationalism was one of the worst consequences of the great depression, but it was also one of its causes. European countries argued with each other instead of finding solutions to their common problems. The United States gave a low priority to trade, and favored tariffs.

We can act cooperatively. This weekend the IMFC, representing 185 countries, endorsed an action plan formulated on Friday by the G7. The centerpiece of this plan is a stronger than ever commitment to use all available tools to support systemically important financial institutions. The plan outlines specific mechanisms that countries can use to support the system, jump-start credit, and restore confidence.

The IMFC also asked the Fund to take on a special responsibility. It recognized that the Fund is a unique institution for this moment, with universal membership, core macro-financial expertise, and a mandate to promote international financial stability. Therefore the IMFC asked the Fund to take the lead in drawing lessons from the crisis and in recommending actions to restore confidence and stability.

The IMFC asked us to begin immediately, so I will begin right now. To restore confidence and stability, we need government intervention in the financial markets which is clear, comprehensive and cooperative between countries. I have suggested in recent weeks that action should be governed by a few simple principles.

First, government action needs to have a clear objective so that effective oversight of how public money is used is possible. This has not always been the case.

Second, national plans need to be comprehensive: they must contain guarantees to depositors and assurances to creditors that are sufficient to ensure that markets function; they must deal with distressed assets and provide liquidity; and most importantly they must include bank recapitalization. The Fund has been advocating this for several months. It seems that now we are all of the same opinion.

Third, action should be fair, in that taxpayers should be able to share upside gains once the crisis passes. IMF experience in 122 banking crises shows that if a crisis is managed well the net cost to the taxpayer can be close to zero, or even better.

Finally, action should be coordinated, at the global level and at the regional level when appropriate—as was done yesterday in the euro zone.

Let me expand on this last principle, because promoting international monetary cooperation is the very first responsibility of the IMF. It is in Article I of our governing document.

International cooperation has not been good enough. Until this weekend, the collapse in confidence in the markets has been almost matched by a collapse in confidence between countries. We saw a very bad trend toward unilateral measures taken with national interests in mind.

Now things are beginning to turn around. Last week we saw coordinated moves by major central banks. This weekend we have gone much further: we have a G7 plan which envisages action on all of the major financial market issues; we have the endorsement of that plan by the entire international community; and, last but not least, we have an action plan in the euro zone.

But we still have a very long way to go. We don't all need to have the same policies, but we must all talk to each other about our policies, and consider the effects of our actions on our partners. This weekend is just the beginning of a long effort.

Let me turn to the global economy.

Action in the financial markets is essential, but it is not sufficient. We also need to deploy all of the instruments of modern macroeconomic policy to limit the damage to the real economy.

For the advanced economies, this means using fiscal policy when they can. The most obvious use of fiscal policy is precisely to ease pressures where they are greatest: in the financial and housing sectors. But governments that can afford it should also be ready to undertake a broader fiscal stimulus.

There is also scope to use monetary policy to support growth, building on the collaborative easing that we have seen this week.

Emerging economies have differing degrees of freedom to act. Some can afford to draw reserves down to finance a temporary and sudden shortfall in capital flows. Others will need to raise policy interest rates in line with rising risk premia to stem outflows and bolster confidence in their currencies.

Some may need help, and possibly very substantial help. The IMFC called on the Fund to offer financial support to members that need it, and we will heed that call. In fact, we have activated emergency procedures to respond quickly to urgent requests, with high access financial programs, based on streamlined conditionality that focuses on crisis response priorities. And to do that, we have plenty of liquidity.

Developing countries need help too. They face reduced export demand and reduced access to trade credit. And many are already suffering from the other crisis—the food and fuel crisis that has strained budgets and balances of payments, and raised inflation and living costs.

The Fund will support you, and I know the World Bank will too, under the great leadership of my friend Bob Zoellick. Together, the Fund and the Bank are already providing advice, technical assistance and financial support. The Fund has increased financing to many countries. We have also changed our Exogenous Shocks Facility so that we can provide assistance more quickly, in larger amounts, with more focused conditionality, and more flexibly.

The rest of the world must also help. I understand that the budgets of advanced countries will be under more strain because of the financial crisis. But it is very important that donors do not respond to the crisis by cutting aid to the poorest and most vulnerable people in the world.

Now, let's look beyond the crisis.

Part of the process of drawing lessons from the crisis is to consider what we need to change in the financial sector and in the financial architecture. Let me take these in turn.

The crisis in financial markets is the result of three failures: a regulatory and supervisory failure in advanced economies; a failure in risk management in the private financial institutions; and a failure in market discipline mechanisms.

Preventing a recurrence of these failures will require an international effort, because borders do not confine financial institutions or keep out financial turmoil.

The Fund can help in coordinating this effort, drawing on the expertise of others. Why the Fund? Two reasons: first, with our universal membership and demonstrated financial diplomacy (for example our work this year on Sovereign Wealth Funds) we can bring together the different actors to discuss risks to global stability and policy responses; and second, we have the machinery for follow up through bilateral surveillance and additional FSAPs.

Let me now talk about the financial architecture, where we have also seen some failures. To prevent a recurrence of these, I see a need to enhance the effectiveness and the legitimacy of the system.

To enhance effectiveness we need better coordination and fewer overlaps between international organizations and better follow up on international agreements. Something as simple as a secretariat to follow up the meetings of the "Gs" could be very useful.

To enhance legitimacy we could add some countries to the existing groups, but I think we need to go further. We need greater reliance on multilateral institutions with near universal membership, so that all countries that are affected by crises have a voice in resolving them.

I will end with a word on Fund reform.

Of course, if we are going to rely more on multilateral institutions, they will have to be representative as well as universal. In the case of the Fund, the reform of quotas and voice that you approved on April 28 is very important. It is a dynamic reform that will continue to produce results over time. We are also undertaking broader governance reform, working with the Board and with the help of Trevor Manuel and his colleagues.

Governance reform is part of a comprehensive program to refocus and modernize the Fund.

We are improving the way we conduct surveillance to emphasize cross-country and macro-financial linkages.

We are reforming our facilities, to make them more useful to members.

In March next year we will hold a conference in Tanzania to discuss how Africa is changing and what the Fund can do to help Africa flourish.

We are changing the way we offer technical assistance, opening new regional centers, and putting in place a system of charges for our work, based on countries' income levels.

We have reached agreement on a new income model, which will put the Fund's finances on a sustainable footing for years to come.

As many of you know, alongside our refocusing efforts, we are completing a restructuring and downsizing of the Fund. I want to thank the staff—both those leaving and those staying—for the flexibility and dedication they have shown during this transition. I also want to thank my management colleagues, the Executive Board, and you, our Governors, for the support that you have given to our work over the past year.

Let me conclude by returning to the point I made earlier. We can emerge from this crisis so long as we act quickly, comprehensively, and cooperatively. The Fund will do its part. But much will depend on you: finance ministers and central bank governors, representatives of your countries, to take the actions needed to restore confidence and stability.

When we meet again in Istanbul in a year's time, let it be said that this weekend in October 2008, the international recovery began, because the nations of the world, gathered together at the Annual Meetings of the International Monetary Fund and the World Bank, chose to act together to create a better world.

Thank you very much.