

**Statement by the IMF Managing Director on
The Role of the Fund in Low-Income Countries
October 2, 2008**

1. ***Progress in recent years but challenges remain.*** In my first year as Managing Director, I have been greatly encouraged by the extent of economic progress underway in many low-income countries (LICs). Growth is strong and poverty is on the decline. At the same time, I have also become more acutely aware of the many challenges still ahead. The current surge in the prices of food and fuel, for instance, as well as recent natural disasters, have put at risk earlier gains in alleviating poverty and controlling inflation. This illustrates the continued vulnerability of many LICs.

2. ***A valued partner.*** I have listened carefully to our member countries on what the Fund can and should do to help them strengthen their economies. The Fund remains a highly valued institution; indeed many have called for more Fund involvement rather than less. I have also benefited from the exchange of views with other stakeholders, development institutions, and Executive Directors, in particular at the recent Board meeting on the role of the Fund in low-income countries. Having reflected on these discussions, and as we head into the Annual Meetings, I want to present my preliminary views on this important part of the Fund's work, and propose an agenda for the medium-term.

Our strategic role

3. ***A fundamental mandate.*** The Fund was created to help countries integrate into the world economy, and thereby contribute to the promotion of growth and development in member countries. This role remains as relevant as ever, in particular for the many LICs in Africa and elsewhere around the world. As countries seek to improve their economic management, and take advantage of the opportunities for international trade and financial flows, including aid, the Fund must be there to support these efforts as it shares its expertise and assists in meeting balance of payments problems.

4. ***Underlining comparative advantage but working with others.*** A key theme of my first year at the Fund has been the need for our institution to refocus on its core competencies related to macroeconomic and financial issues and policies; and to excel within this mandate. In this context, I want to emphasize that, while the Fund is not a development institution—in the sense that it does not provide advice and financing aimed directly at such goals as poverty alleviation, education, or infrastructure—it is an institution that does play a key role in supporting development. The Fund's focused advisory, financing, and capacity building work is essential for LICs to be successful in achieving their development objectives, including the MDGs—reflecting the critical role of a stable macroeconomic environment for growth and development. This specific role of the Fund calls for effective collaboration with our development partners, as we depend on each other's expertise, and as reforms in different

areas are intertwined. In addition, let me underscore that, while the Fund has a wealth of experience and expertise, we must continue to listen and learn from others—above all, from the LICs themselves.

5. ***Promoting macroeconomic and financial stability.*** The role of the Fund in promoting growth has been much debated, and I believe a broad consensus can be identified. A central advantage of the Fund is its ability to connect developments and policies in the real sphere with those in financial and macroeconomic areas. For LICs, the key challenge remains to overcome poverty, in particular by building the institutions and infrastructure for sustainable growth. The linkages between these objectives and the Fund’s work in promoting macroeconomic and financial stability are manifold. Fund advice, while focused on its core areas of expertise, must be informed by a thorough understanding of these broader linkages. In situations of entrenched macroeconomic instability, adjustment measures may be needed in the short run to restore stability, since policies need to be put on a sustainable basis in order to restore growth prospects over the medium-term.

6. ***A changing landscape but the same ultimate objective.*** Over the past decade, however, many LICs have overcome these initial problems, and the central questions for the Fund have shifted. Relevant issues now include how to engrain stability in stronger macroeconomic and financial institutions to boost confidence and hence private investment; how to support financial sector development while ensuring its soundness; and how to scale-up spending for investment and social priorities without jeopardizing debt sustainability. In all these areas of our work, there is no contradiction between saying, on the one hand, that the ultimate objective is to foster broad-based and sustainable improvements in living standards for our member countries and, at the same time, insisting that our specific contribution to that goal must be focused on our core mandate and competencies.

7. ***Tailoring advice to country circumstances.*** This discussion of the Fund’s role in promoting growth in LICs brings me to another key strategic imperative. While the Fund has fundamentally the same responsibilities and basic objectives for all its member countries, the precise tools and the way the work is done must be tailored to the circumstances of countries and country groups. For LICs, these include: widespread poverty; often severe administrative, technical, and data constraints—especially in post-conflict situations; vulnerabilities to economic volatility and debt distress; underdeveloped infrastructure and financial markets; and reliance on aid from development partners. These characteristics imply a need for coherence between macroeconomic and development strategies to foster achievement of the MDGs. They also justify the Fund’s use of dedicated instruments, guidance, and work practices for LICs, while also recognizing the diversity and shifts within this broad group, and with a strong emphasis on capacity building.

8. ***Our mission.*** In order to support clear communication on this part of the Fund’s work, I am presenting the following mission statement for the role of the Fund in LICs (Box

1). The statement incorporates feedback we have received on earlier drafts, and I believe it reflects widely shared views among the membership.

Box 1. Mission Statement for the Fund's Work in LICs

The IMF's mission with regard to low-income countries is to help these countries achieve the macroeconomic and financial stability needed to raise growth and reduce poverty.

As with other members, the Fund provides its LIC members with policy advice, targeted support for capacity building, and, where appropriate, financial assistance. The Fund focuses on its core areas of expertise, namely macroeconomic stabilization and fiscal, monetary, financial, and exchange rate policies, and underlying institutions and closely related structural policies.

At the same time, in responding to low-income countries' particular and evolving needs, the Fund applies specific approaches and instruments. The Fund's work is supportive of countries' own poverty reduction and development strategies, with the underlying objective of helping countries graduate to middle-income status. The Fund helps its low-income members put in place macroeconomic policies and institutions to ensure macroeconomic stability, and to achieve stability in a manner that is conducive to sustained growth and poverty reduction. Building on cross-country experiences and rigorous analysis, and taking into account countries' often limited implementation capacity, the Fund provides:

- (i) advice on macroeconomic policies and institutions that support internal and external macroeconomic stability, including debt sustainability, foster broad-based and sustained economic growth, and enhance integration in the international trade and financial system;
- (ii) assistance for well-sequenced reforms in building capacity and institutions for sound macroeconomic management and financial stability; and
- (iii) concessional financial support.

Fund support for its LIC members calls for continued effective collaboration with the international community, including development institutions and donors, to ensure that the Fund's work is coordinated with the international effort to reach the Millennium Development Goals.

The way forward

9. ***A notable track record.*** Much has been achieved over the past decade to strengthen the Fund's work in LICs. The Fund, with the World Bank, has spearheaded the provision of large scale debt relief, as well as the systematic use of debt-sustainability analysis to guide new borrowing and lending decisions. Fund financing for low-income countries has been supportive of the countries' broader development strategies, through the PRGF and the PRS approach. With the introduction of the PSI, the Fund has responded to calls from mature stabilizers for a nonfinancial instrument to support their policy framework and deliver a clear signal on the quality of their policies. Fund policy advice and program design has become more geared to the effective use of all aid over time. Also, steps have been taken to ensure greater focus and parsimony in program conditionality. Most recently, as part of our broader efforts to help countries manage the current food and fuel price shocks we have modified the Exogenous Shocks Facility (ESF), to make it more flexible and allow for its rapid use.

10. ***Maintaining our effectiveness.*** But we need to step back and take a fresh look at the continued appropriateness of our instruments in a changing world economy. One overarching concern is the need to accommodate the increasing diversity across LICs in a rapidly changing and more challenging global environment. We should retain the capacity to provide sustained financial support that helps countries overcome entrenched balance of payments weaknesses and problems of debt distress, coupled with policy programs that address the underlying weaknesses in policies and institutions. But, over the medium term, as countries develop, fewer should need recourse to this form of assistance. Rather, the Fund will be needed increasingly to help countries integrate into the world economy and manage the shocks from global market volatility and contagion. That, in turn, calls for a focus on helping to build robust macroeconomic policy regimes that provide greater resilience to global economic and market developments. This gradual shift in priorities will take place against a background in which the Fund's budgetary realities imply a shrinking resource envelope for its work on LICs. Efforts to maintain our effectiveness will therefore involve increased prioritization and efficiency in our operations.

11. ***A forward-looking reform agenda.*** A range of initiatives will help the Fund evolve and stay effective in its work on low-income countries. Some of these have already been set in motion; others are new.

- ***LIC lending role.*** The upcoming facilities review provides a timely opportunity to ensure that the Fund has the right tools. The PRGF remains an appropriate instrument for most LICs in need of Fund financial support, in view of their protracted macroeconomic and balance of payments problems, and should remain a central pillar in our LIC architecture. However, the Fund is less well equipped to address some of the demands of its more advanced low-income members. The recent revision of the ESF—which allows for short term-financing in response to exogenous shocks, including for countries with a PSI—fits well in this policy agenda. The broader

facilities review should consider the possible usefulness of a more comprehensive framework for providing short-term financial assistance to LICs, and the scope for streamlining the range of instruments.

- ***Assessing PSI.*** The upcoming review of the PSI—an instrument that has been well received—should allow us to fine-tune this instrument on the basis of experience so far, and ensure that it can meet the needs of an increasing group of LICs that require intensive policy engagement rather than long-term financing.
- ***Assisting fragile states.*** Following the review of facilities, we will present a revised proposal for more proactive and tailored support to fragile and post-conflict states, drawing on the guidance provided by Executive Directors at our discussion last spring.
- ***Maintaining analytic excellence.*** Our work in helping countries respond to shocks goes well beyond the creation of new instruments. In most cases, it will entail providing tailored policy advice to help them safeguard macroeconomic stability to support growth while protecting the poor, backed up by appropriate financial support to facilitate the necessary adjustments. Our response to the food and fuel price crisis has been a good example of this. But we must continue to develop the analytical underpinnings for our policy advice as the needs of our members evolve. Upcoming challenges include helping countries establish more effective monetary and exchange rate regimes for managing shocks to inflation, and medium-term fiscal frameworks that provide an anchor for budget-setting across the cycle. The Fund will also continue to support efforts to enhance stability and predictability in the delivery of foreign aid, in line with the recent Accra Agenda for Action.
- ***Cross-country perspective.*** Our surveillance work for LICs will be informed more systematically by cross-country analysis. For example, the experience of emerging markets provides useful lessons for countries that are starting to tap international financial markets and opening up their financial system. We will also develop analytical approaches that allow us to assess external stability and exchange rates in the particular context of a LIC economy. Fund analysis will provide a regional perspective, and can be particularly helpful in guiding efforts toward greater regional integration. In delivering policy advice, we will put increased emphasis on outreach and political economy considerations in our member countries.
- ***A focus on debt sustainability.*** The Fund will support members to build the policy frameworks and capacity to benefit from new sources of financing. The growing importance of new creditors calls, in particular, for a fresh look at our work to help ensure sound borrowing and lending practices. We will broaden our outreach and seek to refine our analytical tools within the debt sustainability framework. We will also assist countries to strengthen the monitoring, control, and transparency of

expenditures based on new sources of financing and income, including aid and natural resources, to ensure their proper use.

- **Capacity building.** An indispensable part of the Fund's work in LICs will continue to be capacity building. On many issues, the Fund is a unique source of training and technical assistance. Within the Fund's reduced budgetary envelope, special efforts have been made to safeguard assistance for LICs. The challenge is to deliver capacity building with greater prioritization (based on the Fund's core competencies and a focus on strategic guidance). The creation of new regional centers such as the AFRITACs and CAPTAC and topical trust funds through fundraising and partnerships with donors, should allow the effectiveness of our programs to be maintained or even enhanced despite the resource constraints that we face.

12. **Improved coordination.** I am committed to respond to this prioritized agenda within the resources assigned to low-income work in the new medium-term budget. To do so will require improved coordination and work practices, however. In this context, the new LIC unit will play a central role. This unit will be at the forefront of emerging issues relevant to LICs and coordinate LIC work across the Fund. More effective collaboration will also encourage synergies across country teams and departments.

13. **Effective collaboration.** Success also hinges on strong collaboration with development institutions, agencies and donors, and more effective communication generally with all stakeholders. Our recent collaboration with the UN High-Level Task Force on the Global Food Crisis highlights the benefits of a cooperative approach in addressing global problems. I strongly support the current efforts to strengthen our working relationship with the World Bank, based on a clear mutual division of labor. Overlaps in responsibilities should be avoided, such that each institution relies on the other for work within its core areas. In this context, I look forward to the full implementation of the country level agreements envisaged in the JMAP. Our mission statement outlines a clear role for the Fund and provides a basis for more effective communication. This must be a two-way process that includes listening and learning as well as explaining and convincing. Resident representatives will continue to play a key role in explaining the work of the Fund in LICs, including to domestic civil society. I am convinced that greater understanding of the role and relevance of the Fund in LICs is critical for enhancing our effectiveness in supporting stability and prosperity.

14. **Moving forward.** The time has come to move from philosophy to implementation. We may continue to have differing ideas and opinions on how to carry out our role in certain respects, such as the design of Fund facilities, but I believe we can address these and find common ground as we proceed. Our low-income members have pressing needs, and we must set about responding to them promptly and creatively in the months ahead.