INTERNATIONAL MONETARY FUND

Biennial Review of the Implementation of the Fund's Surveillance and of the 1977 Surveillance Decision: Framework and Conduct of Surveillance in 2000-01

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(In consultation with the International Capital Markets, Research, and other Departments)

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Contents Page

Appendix Tables

I. INTRODUCTION

1. Fund surveillance has evolved substantially since the adoption of the Second Amendment to the Articles of Agreement and the 1977 Surveillance Decision. While the purpose of surveillance has not changed, its conduct has been modified significantly. These modifications have represented efforts to adapt surveillance to a changing international environment to maintain, and, where possible, strengthen its effectiveness. Transformations in the conduct of surveillance have been particularly numerous since the mid-1990s, reflecting a broader initiative to strengthen the architecture of the international financial system. As a result of these transformations, the framework of surveillance has broadened substantially in terms of coverage, tools and modalities.

2. The broadened framework of surveillance has posed serious challenges for implementation: it has complicated the task of maintaining a proper focus in surveillance activities; it has required new information and expertise to cover issues outside the Fund's traditional focus on macroeconomics; it has created a need for efforts to integrate the various elements of surveillance; and it has resulted in additional pressures on staff and Board resources.

3. This paper takes stock of the broadened framework of surveillance and examines how surveillance in 2000-01 has coped with the challenges arising from this framework. In addition, various aspects of Article IV consultation procedures are discussed against the background of the recent experience with consultation procedures and the proposals set forth in the paper on Proposals for Reducing Work Pressures.

II. THE EVOLVING FRAMEWORK OF SURVEILLANCE

A. Introduction

4. This chapter will retrace key aspects of the evolution of surveillance. Its central thesis is that this evolution can be understood as a logical outcome of successive attempts to adapt surveillance to changes in the global economic environment in order to maintain and, where possible, strengthen its effectiveness. The chapter's objective is to take stock of these adaptations, outline the key elements of the present framework of surveillance, and present the rationale for the current state of affairs. This analysis will provide the background for the following chapter's review of the implementation of surveillance in 2000-01. The chapter covers the three modes of surveillance, i.e. bilateral, regional, and multilateral surveillance, which all have evolved in response to global economic developments.

5. The chapter is organized as follows. Section B reviews the purpose and principles of surveillance. Section C briefly depicts the major changes in the global economic environment since the late 1970s that have influenced the conduct of surveillance. Section D, which is the heart of the paper, describes the evolution of the coverage (e.g., macroeconomic policies, structural policies, capital account and external debt issues, financial sector issues, institutional issues), tools (e.g., economic data, cross-country analysis, financial market intelligence, indicators of external and financial vulnerabilities, Financial System Stability

Assessments, Reports on Observance of Standards and Codes), and modalities (e.g., multilateral surveillance, regional surveillance, publication of surveillance documents). Section E concludes.

B. Purpose and Principles of Surveillance

6. The purpose of Fund surveillance is set forth in Article IV of the Articles of Agreement, which describes the essential purpose of the international monetary system, defines members' obligations as regards the conduct of their economic and financial policies, and charges the Fund to oversee the international monetary system and members' compliance with their obligations.

7. To further "the continuing development of the orderly underlying conditions that are necessary for financial and economic stability", Article IV requires each member to collaborate with the Fund and other members to assure orderly exchange arrangements and to promote a stable system of exchange rates. Specifically, a member shall (i) endeavor to direct its economic and financial policies toward the objective of fostering orderly economic growth with reasonable price stability; (ii) seek to promote stability by fostering orderly underlying economic and financial conditions and a monetary system that does not tend to produce erratic disruptions; (iii) avoid manipulating exchange rates or the international monetary system in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage; and (iv) follow exchange policies compatible with these undertakings. Viewed from the perspective of the period during which the Second Amendment was drafted, i.e. the period following the collapse of the Bretton Woods system, the purpose of Fund surveillance can be seen as fostering discipline over exchange rate policies in replacement of a rules-based system of stable but adjustable par values.

8. The principles of Fund surveillance are outlined in the 1977 Surveillance Decision.[1] From a practical perspective, key elements of these principles are that the Fund's appraisal of a member's exchange rate policies shall (i) "be based on an evaluation of developments in the member's balance of payments, including the size and sustainability of capital flows, against the background of its reserve position and its external indebtedness"; (ii) "be made within the framework of a comprehensive analysis of the general economic situation and economic policy strategy of the member, and shall recognize that domestic as well as external policies can contribute to timely adjustment of the balance of payments"; and (iii) "take into account the extent to which the policies of the member, including its exchange rate policies, serve the objectives of the continuing development of the orderly underlying conditions that are necessary for financial stability, the promotion of sustained sound economic growth, and reasonable levels of employment." With one exception and apart from minor amendments due to procedural changes, the 1977 Surveillance Decision has been left unchanged since its adoption. The one exception was the introduction in 1995 of explicit references to the size and sustainability of capital flows (see item (i) above).

[1] See Appendix I.

9. Thus, the 1977 Surveillance Decision established that Fund's surveillance over exchange rate policies requires a comprehensive assessment of a member's economic conditions and policies. It also recognized the importance of adapting "surveillance to the needs of international adjustment as they develop." Furthermore, the 1977 Surveillance Decision put the ultimate objectives of financial stability and sustained sound economic growth at the heart of policy assessments under Fund surveillance. Interestingly, from the very beginning, the principles of Fund surveillance under Article IV were seen to mean that Fund surveillance had a crucial role to play in crisis prevention.[2]

C. The Changing Environment of Fund Surveillance

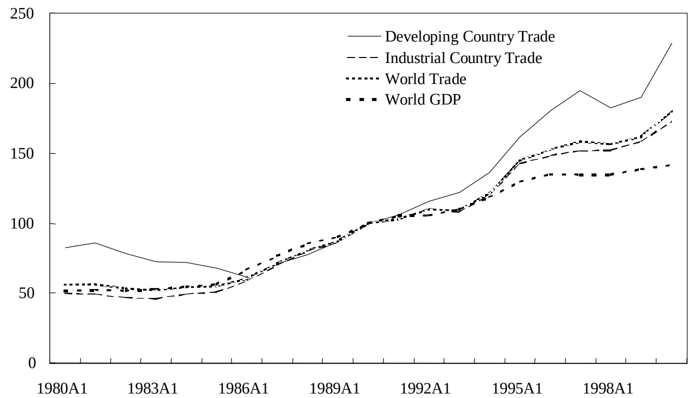
10. While the evolution of Fund surveillance in the past twenty-five years reflected a variety of causes, two important factors stand out: the rapid economic and, particularly, financial integration of member countries; and the expansion of the Fund's membership to a nearly universal coverage.

11. The past quarter century has seen a dramatic intensification of international trade and financial links. World trade grew by more than 10 percent annually between 1980 and 2000 (Figure 1), raising the ratio of world trade to world GDP from 40 percent in 1980 to 48 percent in 2000.[3] Even more spectacular has been the expansion of international capital flows: cross-border transactions in bonds and equities in the major advanced economies were less than 10 percent of these countries' aggregate output in 1980, but exceeded 100 percent by 1995; gross external borrowing of emerging market economies rose more than fivefold from the first half of the 1980s to the second half of the 1990s (Figures 2, 3, and 4)—with the private sector, including financial institutions, accounting for a very large share in the 1990s; and equity financing into emerging market economies rose from an average of less than $1 billion in the first half of the 1980s to an average of $25 billion in the second half of the 1990s.

[2] For instance, the staff documents prepared for the 1980 and 1982 biennial surveillance review indicated that "in the main [the] purpose [of surveillance] is to prevent the build-up of severe external imbalances that would in time make the need for disruptive adjustment measures unavoidable"; and that "because of their regularity and frequency, Article IV consultations are a particularly appropriate instrument for an early identification of balance of payments adjustment needs[, which] in turn could lead to early adjustment, requiring less strenuous corrective measures and increasing the chances of their successful implementation."

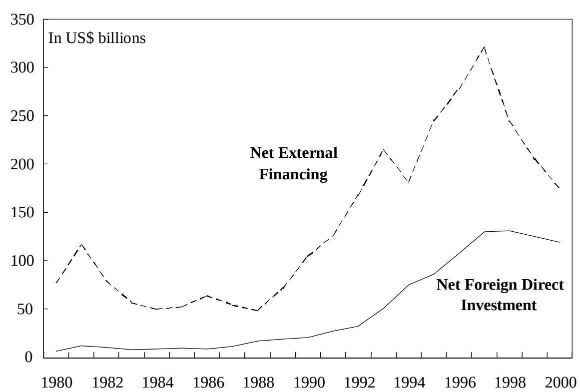
[3] The ratio of world trade to world GDP is defined as the sum of all countries' exports and imports over world GDP.

Figure 1. World Trade 1980-2000



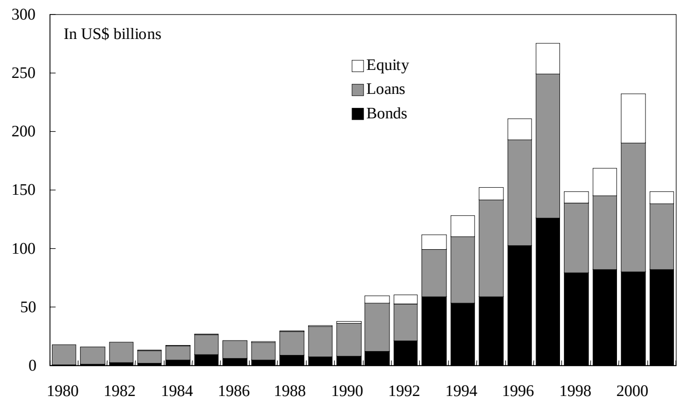
Source: World Economic Outloook

Figure 2. External Financing in Emerging Countries



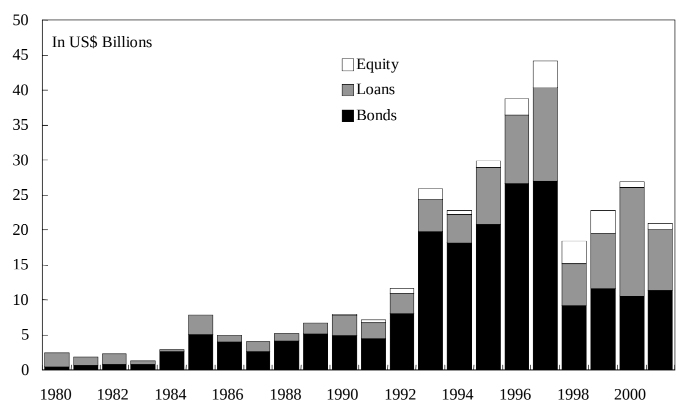
Source: World Economic Outlook

Figure 3. Gross External Financing by Emerging Countries



Source: BEL / Capital Data

Figure 4. Gross External Financing by Emerging Country Banks



Source: BEL / Capital Data

12. In parallel with the growing integration of member countries, the Fund's membership expanded and became nearly universal. In particular, following the collapse of centrally planned economies in Central and Eastern Europe, the Baltic countries, Russia, and other former republics of the Soviet Union, more than 20 transition countries joined (or re-joined) the Fund in the early 1990s.[4]

13. As discussed in greater detail in the next section, these global developments had a profound impact on Fund surveillance. Accession to the Fund of a large number of countries with severe structural and institutional weaknesses further raised the profile of these issues in surveillance. The expansion of capital flows, their effects on emerging market countries' financial institutions intermediating foreign sources of finance, and their impact on the nature of balance of payments crises placed capital account issues, financial sector issues, and, generally, vulnerabilities to external or financial shocks (including shifts in market sentiment) at the heart of surveillance. In addition, timely provision of comprehensive and accurate data became more important than ever before.

14. Crises, particularly the capital account crises experienced by a number of emerging market countries in the second half of the 1990s, were an important catalyst for change. They prompted inquiries into the possible failures of surveillance and sparked initiatives to strengthen it (Box 1). Overall, as stated in the 1977 Surveillance Decision, Fund surveillance did "adapt to the needs of international adjustment as they develop."

D. The Evolving Framework of Surveillance

15. The adaptation of Fund surveillance to a changing environment has affected its coverage, its tools, and its modalities. Changes on these three fronts are outlined below.

Coverage of Surveillance

16. The evolution of the coverage of surveillance can be roughly characterized as the successive addition to an initial focus on exchange rate, monetary, and fiscal policies of four sets of issues: structural policies; capital account issues, including external debt sustainability; financial sector surveillance; and institutional issues.

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[4] Poland was readmitted as a Fund member in 1986, i.e. before the fall of the Berlin wall. Czechoslovakia was readmitted as a Fund member in 1990, ceased to be a member in 1993, and was succeeded to the membership in the Fund by the Czech Republic and the Slovak Republic. Yugoslavia was an original member of the Fund, ceased to be a member in 1992, and was succeeded to the membership in the Fund by Croatia (1993), Slovenia (1993), FYR Macedonia (1993), Bosnia and Herzegovina (1995), and FR Yugoslavia (2000).

Box 1. External Crises and Surveillance Initiatives

Major external crises have typically led to intensive soul-searching on the causes of the crises and on the actions that could be taken to reduce the risks of similar crises in the future. Several initiatives to strengthen surveillance can be linked directly to the evaluation of the debt crisis of the 1980s, the Mexican crisis of 1994, and the Asian crisis of 1997/98.

The Debt Crisis (early 1980s)
The severe external debt-service difficulties experienced by a number of members, including Mexico, were at the center of the 1983 surveillance review. Considering the lessons of the crisis for surveillance, the Executive Board focused on two issues: the ***frequency of Article IV consultations*** and the ***coverage of external debt developments*** in consultation reports. In view of the speed at which debt-servicing problems had spread and past delays in conducting Article IV consultations (in Mexico, the two Article IV consultations prior to the outbreak of the debt crisis had been 27 months apart), Executive Directors agreed on procedural changes to help guarantee a stricter approach to the scheduling of consultations. In addition, Executive Directors indicated that Article IV consultation reports should contain improved reporting of external debt developments in individual member countries and include a description of the medium-term external debt outlook for the country concerned.

The Mexican Crisis (1994/95)
The 1995 biennial surveillance review took place shortly after the external crisis that erupted in Mexico in late 1994. The Executive Board stressed that the growth in cross-border capital flows had presented new challenges to surveillance, that events in Mexico had illustrated the speed and intensity with which international capital markets could react to developments in one country and spread their impact to others, and that the episode underscored the importance of improving surveillance so as to try to prevent such crises from occurring. The Executive Board discussions on enhancing the effectiveness of surveillance focused on the importance of ***timely and comprehensive information from member countries***, the need for greater ***continuity in the surveillance process***, the quality of exchange rate policy discussions, the need to take into account ***financial market developments***, and the candor of staff's policy appraisals. The Executive Board agreed on the inclusion of explicit references to the size and sustainability of capital flows in the 1977 Surveillance Decision, more frequent informal meetings on country matters, and the implementation of a strategy to strengthen data provision to the Fund. In this context, the Executive Board also discussed a possible code of conduct for publication of economic and financial information. These discussions eventually led to the establishment of the Special Data Dissemination Standard in March 1996, which turned out to be the first element of the Fund's work in the area of standards and codes.

The Asian Crisis (1997/98)
In April 1998, the Executive Board reviewed economic developments and policies in a selected number of emerging market economies in 1996/97 and drew five main lessons for Fund surveillance: the effectiveness of surveillance depended critically on the ***timely availability of accurate information***, including data on reserve-related liabilities and short-term debt; the focus of surveillance needed to extend beyond the core short-term macroeconomic issues, while remaining appropriately selective—in particular, close ***surveillance over financial sector and capital account issues*** was necessary; greater attention needed to be paid to the risks of contagion and policy interdependence; the crucial role of policy credibility in the restoration of market confidence underlined the importance of ***transparency***; and effectiveness of Fund surveillance depended crucially on the willingness of members to take its advice. The Asian crisis spurred a broad array of initiatives to strengthen the architecture of the international monetary system, which, were expected to have profound consequences for the conduct of surveillance. These initiatives included strengthened data provision to the Fund, particularly regarding data on reserves, reserve-related liabilities, and short-term debt; the Financial Sector Assessment Program and the development of macroprudential indicators, the development of standards and codes, the creation of Reports on Observance of Standards and Codes, and the development of guidelines on public and external debt management, new publication policies for Fund country-related documents, and the introduction of high-frequency assessments of vulnerability in emerging markets.

Exchange Rate and Other Macroeconomic Policies

17. Macroeconomic policies have been at the center of the Fund's Article IV surveillance since its inception. As noted above, while surveillance was conceived as an instrument to foster discipline in members' exchange rate policies following the collapse of the Bretton Woods system, it was recognized that exchange rate policies could not be analyzed in isolation. The Fund's appraisal of a member's exchange rate policies required a comprehensive assessment of economic developments and policies.

18. Persistent efforts have been made to strengthen the Fund's analysis of members' exchange rate policies. Analytical work has focused on exchange rate movements among major currencies and on the contribution of major industrial countries' macroeconomic policies to these movements; on the choice of exchange rate and monetary regimes, including in the context of strategies to restore macroeconomic stability; and on the consistency between exchange rate policy, other macroeconomic policies, and institutional features—including access to international capital markets and openness of the capital account.[5] Following calls from the Executive Board, efforts have also been made to increase the candor of discussions of exchange rate regimes and analyses of exchange rate levels in surveillance reports.

19. Placing greater emphasis on the systemic impact of major industrial countries' macroeconomic policies has been seen as another important element of better surveillance, given the growing degree of interdependence between the largest economies and other countries.

Structural Policies

20. Structural policies in industrial countries became a major surveillance issue in the early 1980s, as these countries struggled with persistent fiscal deficits and high and rising unemployment rates, and academic and policy-making circles considered the merits of supply-side economics. This heightened attention to structural issues in developed countries complemented a growing focus on structural adjustment in developing countries, which reflected the limits of exchange rate changes in the presence of distortionary pricing policies (e.g. marketing boards) and complex systems of import taxation and export subsidies, and, more generally, explicit stress on growth-enhancing policies in the wake of the debt crisis.

21. Consideration of structural policies in Fund activities, including in surveillance, gained further prominence following the enlargement of the Fund's membership to Central and Eastern European countries, Baltic countries, Russia, and other republics that became independent after the dissolution of the Soviet Union. In these countries, it was immediately evident that macroeconomic and structural issues were inextricably linked. In recent years, in

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[5] See *Exchange Rate Regimes in an Increasingly Integrated World Economy* by M. Mussa et al., Occasional Paper No. 193, August 2000.

light of developments in the United States, potential growth and productivity issues have gained further prominence in surveillance for advanced economies.

22. Given the vast array of structural problems faced by many member countries, maintaining a proper focus in covering structural issues has long been an important concern for Fund surveillance. Macroeconomic relevance—i.e. only covering issues that have a direct and appreciable influence on macroeconomic developments—eventually became the accepted criterion for decisions on coverage of surveillance.

23. One area of structural policies that, from the start, was recognized as important to Fund surveillance is trade policy. For instance, at the conclusion of the 1983 review of surveillance, Executive Directors stressed the need for the Fund to address the dangers associated with the growth of protectionism; encouraged staff to expand the coverage and analysis of trade policy matters in Article IV consultation reports—while avoiding overlap with the areas of responsibility of the GATT (now the WTO); and indicated that such coverage should be on the impact of trade measures on domestic adjustment of the country imposing these measures and on its trading partners. In the latest review of the Fund's role in addressing trade issues, Executive Directors agreed that the Fund has a mandate to support open international trading system and trade liberalization; and given this principle, that the Fund should continue to address trade issues and support trade liberalization in the context of surveillance and Fund-supported programs where appropriate.

Capital Account and External Debt Issues

24. All issues related to macroeconomic stabilization and adjustment have always been at the center of Fund surveillance. These naturally include the balance of payments, the international investment position, and capital flows. The 1977 Surveillance Decision reflected this consideration, as it specified that "[t]he Fund's appraisal of a member's exchange rate policies shall be based on an evaluation of the developments in the member's balance of payments, against the background of its reserve position and its external indebtedness." This being said, the emphasis placed on capital account issues in the implementation of surveillance substantially increased first in the wake of the debt crisis of the 1980s and again following the emerging market crises of the 1990s.

25. The debt crisis of the 1980s pointed to the need to improve coverage of external debt developments and policies in Article IV consultations and, in particular, to include in reports on borrowing countries a forward-looking analysis of the policies needed to maintain the external debt service profile within appropriate bounds.

26. The emerging-market crises of the 1990s demonstrated that countries with access to international capital markets could be extremely vulnerable to a cessation or reversal of capital inflows, even when there were no doubts as to the ability of the sovereign to service its debt obligations; and that such shifts in capital flows could have severe macroeconomic consequences. These crises focused attention on the size and composition of capital flows, global conditions likely to affect capital flows (e.g., interest rates in the major advanced economies, degree of risk aversion in mature financial markets), contagion, and emerging market countries' vulnerabilities to abrupt changes in market sentiment. As noted above, this

emphasis on capital account developments prompted the 1995 amendment to the 1977 Surveillance Decision, which highlighted the standing of capital account developments in the Fund's assessment of members' exchange rate policies.

Issues Related to the Financial Sector and Non-financial Corporate Sector

27. Financial crises in the 1990s, including the banking crises in Nordic countries in the early part of the decade and the emerging market crises later on, provided a vivid illustration of the strong, two-way links between the health of the financial sector and economic performance. Spurred by these developments, financial sector issues—especially, conditions in the banking system—have gained greater prominence in the Fund's surveillance activities since the mid-1990s and, indeed, have become one of the core areas of Fund surveillance. As discussed below, efforts to strengthen financial sector surveillance were markedly enhanced by the introduction of the Financial Sector Assessment Program in 1999.

28. The experience in emerging-market countries affected by the 1997-98 crisis, particularly in Asia, also demonstrated that balance sheet weaknesses of the non-financial corporate sector could have direct dramatic macroeconomic repercussions, aggravate financial sector problems, and significantly constrain the scope for exchange rate or interest rate adjustment in the face of a shift in market sentiment. Recognizing these links, the assessment of vulnerabilities of the nonfinancial corporate sector increasingly came to be seen as an important complement of financial sector surveillance, although efforts to address these issues have often been stymied by lack of adequate information.

Institutional Issues

29. A broad range of institutional issues, including central bank independence, financial sector regulation, corporate governance, and policy transparency and accountability—which contribute to good public sector governance—became an important element of Fund surveillance in the 1990s. This development can be traced to a conjunction of several factors: the experience in transition economies, which clearly showed that development of well-built institutions and legal frameworks was an essential ingredient of a successful transformation into a market economy; the experience of countries with severe governance problems, which highlighted, *inter alia*, the benefits of fiscal transparency;[6] the adoption of formal inflation targeting regimes and rules-based fiscal policy frameworks by a number of advanced economies; financial sector crises, which pointed to weaknesses in supervisory and regulatory regimes and shortcomings in corporate governance and bankruptcy laws; emerging-market crises, which called attention to external debt and foreign exchange reserve management; and, finally, a growing focus on activities that might undermine the integrity of the international financial system (e.g., money laundering).

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[6] See *Executive Board Reviews IMF's Experience in Governance Issues*, PIN No. 01/20, March 8, 2001.

Tools of Surveillance

30. The extension of the coverage of surveillance has been accompanied by initiatives to improve the tools of surveillance. Effective coverage of additional policy areas in Fund surveillance and strengthened coverage of traditional areas required more extensive, detailed, frequent, and accurate information. It also required appropriate tools to support information gathering and analysis. Fund surveillance has consistently relied on both standardized quantitative tools and qualitative country-specific analysis, with a view to ensuring that surveillance be simultaneously even-handed across the membership and well adapted to the circumstances of individual countries.

31. ***Data provision to the Fund***. Adequate provision of data to the Fund has always been essential for effective surveillance.[7] Over time, with the extension of the coverage of surveillance and the need for more continuous monitoring, data requirements for surveillance have correspondingly expanded.

32. Crises were important catalysts in this process. The debt crisis in the 1980s drew attention to the need for adequate data on external borrowing. Following the 1994/95 Mexican crisis, which showed the high speed at which incipient difficulties could blossom into a full-fledged crisis and highlighted the impact on surveillance of even temporary gaps in data provision, the Executive Board emphasized the importance of receiving comprehensive, high-quality, and timely macroeconomic and financial data. As an absolute minimum, the Board called on members to provide to the Fund on a timely basis a set of key economic indicators and the central bank balance sheet. In recent years, in light of the nature of the 1997/98 emerging-market crises, attention has focused on the timely provision of data on external reserves, foreign currency liquidity, and, again, external debt.[8] In this context, in June 2000, the Board agreed to establish the SDDS prescription for international reserves, foreign currency liquidity, and external debt as benchmarks for data provision to the Fund in these areas. The most recent staff paper on this issue considers data requirements for vulnerability assessments, in light of the considerations that surfaced in the October 2001 Board discussion of vulnerability assessments for emerging market economies.

33. ***Other sources of information*** also gained greater importance as the coverage of surveillance expanded. For instance, strengthened surveillance over capital account developments required paying closer attention to market sentiment, i.e., ***capital market participants' views*** about both global financial developments and the situation of particular countries. The Research Department kept regular contacts with market participants and analyzed financial market data. The creation of the International Capital Markets Department and the establishment of the Capital Markets Consultative Group have further strengthened

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[7] Article IV, Section 3 (b) states that "…the Fund shall exercise firm surveillance over the exchange rate policies of members.." and that "each member shall provide the Fund with the information necessary for such surveillance…"; and Article VIII, Section 5 prescribes that "the Fund may require members to furnish it with such information as it deems necessary for its activities…"

[8] See *IMF Executive Board Reviews Data Provision for Surveillance*, PIN No. 00/59, August 11, 2000.

the collection and analysis of such information for surveillance in countries that are vulnerable to large capital account swings (see below).

34. Covering issues beyond the Fund's traditional areas of expertise, particularly in the structural domain, has necessitated greater ***use of the expertise of other international institutions***, such as the World Bank and the OECD. The Executive Board has instructed staff to be aware of the work done by other institutions and to incorporate the results of this work into the surveillance process, whenever they are relevant to the Fund's concerns. As regards cooperation between the World Bank and the Fund, the Executive Boards of both institutions have stressed the importance of strengthened and more systematic coordination between the Fund and the World Bank to secure the benefit of the complementary areas of expertise of the two institutions.[9] For instance, where appropriate, Fund staff would be expected to draw on analysis of structural (e.g., privatization) and social (e.g., health, education, poverty alleviation) issues within the World Bank's core areas of expertise.

35. ***Tools for exchange rate analysis***. Strengthening the analysis of exchange rate developments has always been critical for Fund surveillance. In 1983, a system was established to track developments in members' ***real effective exchange rates*** and inform the Executive Board on a regular basis of these developments.[10] While formal notifications to the Board were later discontinued, real effective exchange rate series have continued to figure prominently in the Fund's analysis of exchange rate development and policies in member countries.[11] [12]

36. The creation of the ***Coordinating Group on Exchange Rate Issues*** (CGER) in 1995 was another step toward strengthening the Fund's analysis of exchange rate developments. CGER work has focused primarily on medium-run equilibrium levels of exchange rates in industrial countries. These assessments have been used as inputs into staff's analysis of exchange rate issues in both bilateral and multilateral surveillance.[13] Beyond this, various approaches for exchange rate assessments have been used in Article IV Consultation reports,

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[9] See *IMF Concludes Discussion Strengthening IMF – World Bank Collaboration on Country Programs and Conditionality,* PIN No. 01/92, September 9, 2001.

[10] Changes in excess of 10 percent were highlighted through issuance of individual information notices to the Board.

[11] Individual information notices on changes in real effective exchange rates in excess of 10 percent and the quarterly reports on changes in real effective exchange rates were discontinued in 1990 and 1995 respectively, as their value for effective surveillance was perceived to have become marginal.

[12] Real effective exchange rate series are not produced for some members due to a lack of data. For details, see *A Primer on the Fund's Information Notice System*, A. Zanello and D. Desruelle, WP/97/71, May 1997.

[13] For more information, see *Methodology for Current Account and Exchange Rate Assessments,* P. Isard et al., Occasional Paper No. 209, December 2001.

with, recently, more attention to Balassa-Samuelson effects and the distinction between equilibrating and disequilibrating moves.[14]

37. ***Tools of financial sector surveillance***. The extension of the coverage of surveillance to financial sector issues raised a number of questions: How could the Fund bring to the surveillance process the necessary expertise to tackle these issues? What information needed to be collected, and how should it be collected? How should financial sector assessments be structured to bring them to bear on the Fund's Article IV consultations?

38. It was recognized that, while Article IV missions, possibly with teams reinforced by adding financial sector expertise, could attempt to address selected financial sector issues, they could not reasonably be expected to conduct in-depth financial sector assessments. In light of this fact, the joint World Bank-IMF ***Financial Sector Assessment Program (FSAP)*** was introduced in May 1999, first on a trial basis, and, subsequently, on a permanent basis. The purpose of the FSAP was to offer countries a coherent and comprehensive framework for identifying financial system vulnerabilities, ascertaining development needs and priorities, and developing appropriate policy responses.

39. At the discussion of the last review of the FSAP, Executive Directors concluded that the FSAP process had succeeded in providing such a framework and that the Financial System Stability Assessments (FSSAs), which are derived from FSAP findings and discussions conducted during Article IV consultations, had contributed to deepening the coverage of financial sector issues in bilateral surveillance.[15] Consequently, while participation in the FSAP is voluntary, FSSAs have become the preferred tool for financial sector assessments in the context of Fund surveillance.

40. Effective financial sector surveillance requires not only an appropriate framework for analysis but also adequate data. To improve data collection and reporting, a core set of ***financial soundness indicators*** (FSI) for the banking sector and an "encouraged set" of financial indicators for other sectors have been identified.[16] The Executive Board has welcomed these efforts and expressed support for a more systematic compilation of such data in Article IV consultations where in-depth financial sector assessments are undertaken. Where available, data on FSIs should be included in Article IV consultation reports.

41. ***Tools for assessing external vulnerabilities***. The need to assess countries' vulnerabilities to sudden shifts in capital flows prompted a search for quantitative tools to

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[14] See *Real Exchange Rates and Competitiveness: A Clarification of Concepts and Some Measurements for Europe,* L. Lipschitz and D. McDonald, WP/91/25, March 1991.

[15] See *IMF Reviews Experience with the Financial Sector Assessment Program (FSAP) and Reaches Conclusion on Issues Going Forward,* PIN No. 01/11, February 5, 2001.

[16] The sectors covered by the "encouraged set" of financial soundness indicators are the nonbank financial sector, the corporate and household sectors, and real estate markets. The "encouraged set" of indicators also include several banking sector indicators not present in the core set.

support this analysis. In particular, indicators of reserve adequacy based on current account flows were no longer seen as sufficient, even though they continued to provide valuable information. Against this background, the Executive Board considered the use of various ***debt- and reserve-related indicators of external vulnerability*** and concluded that these indicators, notably the ratio of reserves to short-term debt, could be important tools for strengthening the analysis of vulnerability.[17]

42. In circumstances where there are questions about continued access to international financial markets, either because of general market conditions, contagion effects, or the economic situation of the particular country under consideration, ***estimates of*** the country's ***external financing needs*** are of great importance. As part of the quarterly vulnerability assessment exercise for emerging market countries (see below), such estimates are regularly produced.

43. Analysis of high-frequency market ***data on borrowing spreads***, which are available for most emerging market countries, provides valuable information on market sentiment and changing sensitivities to contagion. Such analysis has been more widely used in surveillance. In particular, it is one of the main inputs of the quarterly vulnerability assessment exercise for emerging market countries. The use of information on market developments in surveillance is expected to be strengthened with the creation of the International Capital Markets department.

44. Formal ***Early Warning System*** (EWS) models are also a potentially useful tool for the analysis of external crisis vulnerabilities. While the Executive Board has encouraged staff to discuss the results of EWS models with country authorities and to keep the Board informed of these discussions, it has cautioned that EWS models are imperfect signaling tools and, in particular, suffer from high false positive signal ratios.

45. ***Tools for strengthening the coverage of institutional issues***. The coverage of institutional issues in bilateral surveillance raises questions that are similar to those concerning the coverage of the financial sector. Substantial treatment of these issues requires the relevant expertise to collect and analyze the needed information, the capability to draw from this analysis conclusions regarding the existence of significant institutional weaknesses, and, where relevant, the capacity to arrive at a set of prescriptions for remedial actions.

46. As in the case of financial sector surveillance, efforts to strengthen the coverage of institutional issues in surveillance were paralleled by broader initiatives to help countries evaluate and improve their institutional, legal, and regulatory settings through design of standards and codes and assessments of their observance. In eleven areas, ***standards and codes*** have been identified as useful to the operational work of the Fund and the World Bank: data dissemination, fiscal transparency, monetary and financial policy transparency, banking supervision, securities, insurance, payments systems, corporate governance, accounting,

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[17] See *Debt and Reserve-Related Indicators of External Vulnerability*, PIN No. 00/37, May 19, 2000.

auditing, and insolvency and creditor rights.[18] In these areas, Reports on the Observance of Standards and Codes (ROSCs) provide a systematic framework for organizing and presenting information on institutional issues and, thus, valuable input for Fund surveillance.[19] In other areas, such as public debt management and foreign exchange reserve management, recently developed ***guidelines*** may be used to inform the discussions between the authorities and the Fund on these issues. In particular, they may serve as useful benchmarks for assessments of current strengths and weaknesses.[20] The Capital Markets Consultative Group Report on Creditor-Debtor Relations provides information on best practices regarding investor relations programs, which can help guide staff's work in this area. In still other instances, for example to address anti-money laundering issues, a voluntary ***questionnaire*** has been developed as a possible framework for discussions during Article IV consultations.[21]

47. In addition to the development of the above tools, which were designed to improve coverage of specific areas, efforts have been made to strengthen discussion of many areas of surveillance through greater use of ***cross-country analysis***. For instance, Article IV consultations for several European countries were informed by common cross-country background papers;[22] discussions of external competitiveness have benefited from comparative analyses of the evolution of exports, market shares, and labor costs covering the member concerned and comparable countries; and discussions of financial and external vulnerability have gained from cross-country comparisons of key vulnerability indicators.

Modalities of Bilateral and Regional Surveillance

48. In parallel with the extension of the coverage of surveillance and the development of better tools, continuous efforts have been made to adapt the modalities of surveillance in order to strengthen it. These efforts have focused on four areas: (i) ensuring the continuity of surveillance; (ii) adapting the modes of surveillance to the realities of growing regional integration; (iii) strengthening multilateral surveillance to reflect growing interdependencies;

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[18] In addition to standards in these eleven areas, the Executive Board generally agreed that the Financial Action Task Force (FATF) 40 Recommendations be recognized as the appropriate standard for combating money laundering, and that work should go forward to determine how the Recommendations could be adapted and made operational to the Fund's work. In November 2001, Executive Directors agreed to expand the Fund's involvement beyond anti-money laundering to efforts aimed at countering terrorism financing. See *IMF board Discusses the Fund's Intensified Involvement in Anti-Money Laundering and Combating the Financing of Terrorism,* PIN No. 01/20, November 16. 2001.

[19] See *Assessing the Implementation of Standards—An IMF Review of Experience and Next Steps*, PIN No. 01/17 March 5, 2001.

[20] See *Guidelines for Public Debt Mangement,* IMF Website, November 12, 2001.

[21] See *IMF board Discusses the Fund's Intensified Involvement in Anti-Money Laundering and Combating the Financing of Terrorism,* PIN No. 01/20, November 16, 2001.

[22] Topics of such cross-country papers included exchange arrangements for transition economies on road to EU accession, the policy response in cyclically advanced euro-area economies, and the determinants of job-rich growth in certain European Union countries.

and (iv) enhancing the impact of surveillance. Initiatives relating to bilateral and regional surveillance are discussed in this section, while innovations in multilateral surveillance and efforts to enhance the impact of surveillance are covered in the next two sections.

49. ***Ensuring the continuity of surveillance***. The ability to detect incipient economic difficulties and engage in a meaningful dialogue with national authorities on possible remedies requires continuity in the surveillance process. The importance of continuous surveillance was recognized in the 1977 Surveillance Decision, which established the principle of annual Article IV consultations. However, while the principle of annual Article IV consultations has been re-affirmed on numerous occasions—most recently during the 2000 biennial surveillance review—application of this principle has had to contend with persistent concerns about resource constraints. Consultation cycles and, more generally, consultation procedures thus have been regularly re-examined. In this process, calls for—and actions toward—a stricter adherence to the principle of annual consultations have tended to alternate with moves toward greater flexibility (Box 2).

50. From the inception of the Article IV consultation process, there has been a clear understanding that, in some instances, effective surveillance may call for more frequent than annual discussions with a member. Efforts to use formal procedures for these cases, such as the special consultations envisaged in the 1977 Surveillance Decision or the *ad hoc* consultations contained in the 1979 supplemental surveillance procedures, proved largely unsuccessful because these procedures soon came to be seen as carrying a stigma.[23, 24] Instead, informal contacts between national authorities, staff, and management became the main vehicle for discussions between consultations. In recent years, in addition to regular exchanges of information, staff visits half-way between two Article IV consultations have been routine in a number of countries, particularly in emerging market countries. Informal meetings on country matters provide a channel to inform the Executive Board of significant developments between Article IV consultations. In addition, Post-Program Monitoring (PPM), which was introduced in 2000, provides for close monitoring of economic developments and policies in members with substantial Fund credit outstanding following the expiration of their arrangements with the Fund.[25]

[23] See Paragraph V under “Procedures for Surveillance” in the 1977 Surveillance Decision.

[24] See *Decision No. 6026-(79/13)*, January 22, 1979.

[25] See Chapter IV of *Biennial Review of the Implementation of the Fund’s Surveillance and of the 1977 Surveillance Decision— Surveillance in a Program Environment.*

Box 2. The Evolution of Article IV Consultation Procedures, 1983-1997[1]

1983: The debt crisis, which erupted in 1982 highlighted the speed at which economic problems could spread. Against this background, and in light of prominent cases of long lags between Article IV consultations and a generalized fall in coverage of consultations, the Executive Board agreed to implement procedural changes to guarantee a stricter approach to the scheduling of consultations. These changes included establishing criteria for placing countries on a "strict cycle" (12-month with a 3-month grace period), setting a permissible outer limit of 2 years for the interval between consultations for countries not on the strict cycle, and circumscribing circumstances where delays could be justified.

1987: Motivated by pressures on staff and Board resources, the bicyclic consultation procedure was introduced. This procedure consisted in the conduct of a simplified consultation every second year, involving a shorter staff report, no background documentation, and issuance of the staff report to the Board for information only. Initially, the bicyclic consultation procedure was applied to 23 countries.

1991: In response to the severe pressure on staff resources stemming from work in Central and Eastern Europe and the U.S.S.R., all members except the seven largest industrial countries, program countries, and arrears cases were temporarily moved to longer consultation cycles.

1993: On the occasion of the 1993 biennial review of surveillance, Executive Directors concluded that the intensification of work load pressures had adversely affected surveillance-related activities and that there was a need for greater continuity of surveillance. Given this conclusion and the perception that the bicyclic procedure had not resulted in substantial resource savings, the bicycle procedure was abolished and most countries were placed on the annual consultation cycle.

1995: Requirements for background documentation were relaxed.

1996: A lapse-of-time procedure for concluding Article IV consultations was approved by the Board, with the understanding that the procedure would be used sparingly.

1997: Noting the need to ensure an effective focus of surveillance in the context of strained resources, Executive Directors encouraged flexibility regarding consultation frequency, mission size, and documentation. In particular, Directors agreed that greater use should be made of longer consultation cycles, encouraged staff to inject greater flexibility in deciding the scope of staff reports, and further relaxed requirements for background documentation. In the wake of these decisions, 13 countries were moved to a longer consultation cycle.

[1] See *Silent Revolution: The International Monetary Fund, 1979-1989*, by J. Boughton, Washington: International Monetary Fund, 2001.

51. Surveillance over economic policies in major industrial countries, which are frequently covered in bilateral, regional, and multilateral exercises, has long been characterized by a high degree of continuity. In developing economies, surveillance had usually been less continuous, with the major surveillance exercise being the annual (or biennial) Article IV consultation. For countries without market access, this practice has generally been appropriate, given the nature of shocks and vulnerabilities faced by these countries. However, the crises of the second half of the 1990s have shown that this is insufficient for emerging market countries, which rely heavily on private market financing and are thus vulnerable to shifts in market sentiment. In these countries, effective surveillance requires a high degree of continuity. As discussed in greater detail below, to

keep track of the risks of an external crisis in these countries, a new framework was set up in May 2001 to assess their vulnerabilities to changing market conditions on a monthly and quarterly basis.

52. ***Enhancing regional surveillance***. With members in different parts of the world pressing ahead with regional economic integration—a phenomenon most prominent in Europe but also evident in parts of Africa and the Western Hemisphere, the traditional modes of bilateral and multilateral surveillance were missing an increasingly important level of economic decision-making. To close this gap, contacts between staff and regional economic institutions have intensified, and Board discussions of monetary, exchange rate, and other relevant policies in currency unions (i.e. the euro area, the West African Economic and Monetary Union, the Central African Economic and Monetary Community, and the Eastern Caribbean Currency Union) have progressively expanded. The frequency and degree of formality of these activities have varied across currency unions, with the highest frequency and greatest degree of formality (i.e., formal integration in Article IV consultations with union members) reached for the euro area.

Modalities of Multilateral Surveillance

53. ***Strengthening multilateral surveillance***. Traditionally, the two main pillars of the Fund's multilateral surveillance have been the semi-annual discussions on the World Economic Outlook (WEO) report, and annual discussions on the International Capital Markets (ICM) report. In response to the growing interdependencies among member countries, notably the rapid expansion of financial linkages, the Fund has undertaken significant efforts to strengthen surveillance over capital markets, to enhance the continuity of multilateral surveillance, and to boost the integration of multilateral surveillance and bilateral surveillance.

54. A key initiative to strengthen surveillance over capital markets was the creation of the ***International Capital Markets Department*** (ICM) in 2001. The objective was to deepen the Fund's understanding of capital market operations; improve its capacity for addressing systemic issues related to capital market developments; enhance its capability to provide early warning of potential stress in the financial markets; and strengthen its ability to help member countries gain access to international capital markets. ICM has intensified the collection and analysis of information on developments in international financial centers, and has made this information available to area and other departments. It has also broadened the Fund's liaisons with capital market participants, national authorities, and international fora concerned with capital market issues. Another important initiative to enhance capital market surveillance was the establishment of the ***Capital Markets Consultative Group*** in 2000, which has facilitated high-level contacts between capital market participants and Fund staff.

55. Efforts to enhance capital markets surveillance have resulted in the production and broad dissemination within the Fund of a substantially higher volume of information on capital market developments. This includes the daily *Global Markets Monitor*, which provides information on developments in both mature and emerging markets as well as on

changes in market sentiment; up to 2001, the quarterly report on *Emerging Market Financing*; and, as of the first quarter of 2002, the quarterly ***Global Financial Stability Report*** (GFSR), which replaces the annual *International Capital Markets Report* and the quarterly report on *Emerging Market Financing*. The GFSR was created to allow broader and more continuous surveillance of capital market developments and more frequent reporting to the Executive Board and to the public on multilateral or systemic capital market issues. The report's main objective is to identify potential vulnerabilities in the international financial system from a multilateral perspective and to analyze linkages between developments in mature financial centers and capital flows to emerging markets.

56. To increase the continuity of multilateral surveillance, the ***World Economic and Market Developments*** (WEMD) sessions have been held approximately every six to eight weeks since 1993 to allow staff, management, and the Board to keep abreast of the rapid evolution of global economic and financial conditions. In these sessions, the Economic Counselor has presented to the Executive Board summaries of key global economic and financial market developments and their implications for the outlook and policy requirements. These presentations have been supported by background papers outlining issues for discussion and updating major global developments. In recent years, risks and vulnerabilities emanating from financial markets, and systemic risks, have been an increasing focus of the sessions. In addition, special topics related to multilateral surveillance have been folded into some of the WEMD presentations, including highlights from the latest CGER exercise on exchange rate assessments for industrial countries, discussion of exchange rates in key emerging markets, highlights from early warning system (EWS) models, the rise in oil prices (December 2000), and the shrinking supply of US treasury securities (March 2001). Two mini-WEMD sessions were held in September and October of 2001 to assess the impact of the September 11 terrorist attacks.

57. In line with the recommendations of the external review of surveillance and the conclusions of the 2000 biennial surveillance review, efforts have been made to strengthen the integration of multilateral surveillance with bilateral surveillance. The key initiative on this front was the launch in May 2001 of a ***new framework to keep track of the risks of an external crisis in emerging market countries*** and help assess their vulnerabilities to changing market conditions. This framework was designed to provide a systematic process for high-frequency (monthly and quarterly) monitoring coupling detailed, country-specific knowledge of area departments with expertise and market information of functional departments. Specifically, the assessment of vulnerabilities relies on the following inputs: changes in the world economic outlook, capital market information—including assessment of market access conditions under various scenarios and analysis of borrowing spreads and contagion, estimates of external financing requirements, financial sector vulnerability assessments, results of Early Warning System models, and country-specific expertise of area departments.

58. Other efforts to strengthen the integration of multilateral and bilateral surveillance include greater attention to the implications of the global economic outlook—both baseline and risks—for individual countries in Article IV consultations discussions and other bilateral

surveillance activities, including for countries with limited or no market access for which the key channel of transmission of external shocks continues to be trade developments (e.g., terms of trade, level of foreign demand).

Dissemination of Surveillance Assessments

59. The potential impact of Fund surveillance on members' policies depends critically on the importance members attach to the Fund's assessments of economic conditions, prospects, and policies. To enhance the effectiveness of surveillance, the Fund has persistently attempted to strengthen its ability to persuade members by improving the quality of its advice and providing it on a timely basis. All initiatives described above to adapt the coverage, tools, and modalities of surveillance to a changing global environment are part of this effort. However, it has been clearly recognized that better and more timely advice may not be sufficient to ensure that this advice is taken seriously. Thus, the Fund has also sought to strengthen the channels for transmitting its policy advice. In particular, it has sought to make greater use of peer pressure and to increase transparency.

60. Fundamentally, Fund surveillance is a ***peer review*** of members' economic policies. The output of bilateral surveillance is an assessment of the economic situation and policies of individual members by the whole membership of the Fund through the Executive Board, while the output of multilateral surveillance is a Fund assessment of global economic conditions and needed policy responses. For both bilateral and multilateral surveillance, the first audience is the national authorities of member countries.

61. Peer review of economic policies is also conducted in the context of meetings of the International Monetary and Financial Committee and a number of fora, including the G-7, the Manila Framework Group, the Gulf Cooperation Council, and the Western Hemisphere Finance Ministers Group. Over the years, at their invitation, the Fund has stepped up its participation in these groups' activities, and, in doing so, has striven to strengthen peer pressure for necessary policy changes, particularly by drawing attention to key risks and vulnerabilities in individual economies and globally. Generally, for meetings of these fora, the Fund has contributed surveillance notes providing assessment of policies and risks in the major economies, in the region, and globally; and the Managing Director, the Economic Counselor, or other senior Fund officials have made presentations. Occasionally, at the request of these groups, surveillance notes have also included discussion of specific issues (e.g., in the past two years, global imbalances and adjustment issues, and prospects and risks in emerging market countries).

62. ***Transparency*** in Fund surveillance was long confined to publication of the semi-annual WEO and annual ICM reports and the release of Article IV consultation reports to selected international agencies.[26] Greater transparency in bilateral surveillance was resisted on the basis of concerns that it might lead to less candid discussions between staff and

[26] Publication of the WEO and ICM reports started in 1980.

national authorities. However, gradually, the view gained ground that Fund surveillance would benefit from public scrutiny and would become more effective if Fund views on members' policies were made publicly available in a systematic and timely manner. Against this background, the Fund's policy on transparency evolved over time toward greater provision of information. In 1997, the Board agreed to publication on a voluntary basis of the summings up of Board discussions of Article IV consultations in the form of Press Information Notices, later renamed Public Information Notices. This was followed in 1999 by a decision to allow publication on a voluntary basis of Article IV consultation reports.[27] Other initiatives to increase transparency include efforts by staff missions to meet with a broader set of economic stakeholders (e.g., trade unions) and increase contacts with local media.

E. Conclusions

63. While the purpose of surveillance has remained unchanged, its conduct has evolved profoundly over the past 25 years. This evolution has been the result of continuous efforts to adapt surveillance to changes in the global environment and has affected all aspects of surveillance, i.e. its coverage, tools, and modalities (Box 3). Conducting surveillance in this broadened framework presents important challenges for the focus of surveillance, the quality of its analysis, and the integration of its different elements into a coherent assessment. These issues are addressed in the next chapter.

[27] The initial decision to allow publication of Article IV consultation reports was taken in the context of a pilot project. In 2000, the policy was established on a lasting basis. See *IMF Reviews the Experience with the Publication of Staff Reports and Takes Decisions to Enhance the Transparency of the Fund's Operations and the Policies of the Members,* PIN No. 01/3, January 12, 2001.

Box 3. Evolution of Surveillance—A Summary

Coverage of Surveillance

In addition to focus on exchange rate, fiscal and monetary policies, exchange regime and relevant trade issues

- Coverage of selected structural policies
- Coverage of vulnerabilities to balance of payments or currency crises, with special emphasis on external debt and capital account developments
- Coverage of financial sector issues
- Coverage of selected institutional issues

Tools of Surveillance

Better information collection

- Strengthened data provision to the Fund
- Access to capital market intelligence
- Use of expertise of other international institutions on issues beyond the Fund's traditional areas of expertise

Tools for financial sector surveillance

- Financial Sector Assessment Program
- Financial soundness indicators (ex-macroprudential indicators)

Tools for analysis of crisis vulnerabilities

- Early warning systems
- External vulnerability indicators
- Financing requirement projections
- Analysis of spreads and other financial market information

Tools for analysis of institutional strength

- Reports on Observance of Standards and Codes
- Guidelines on public debt management and foreign exchange reserve management

Tools for exchange rate analysis

- CGER assessments
- INS real effective exchange rates

Modalities of Surveillance

In addition to Article IV consultations at the bilateral level and World Economic Outlook and capital markets reports at the multilateral level

- Staff visits between Article IV consultations
- Frequent informal Board sessions on country matters
- Frequent meetings on World Economic and Financial Market Developments
- High-frequency assessments of vulnerabilities of emerging market countries
- Surveillance at the regional level (e.g., currency unions)

Dissemination of Surveillance Assessments

In addition to peer review by the Board

- Contribution to peer surveillance reviews in regional fora
- Voluntary publication of Public Information Notices (ex-Press Information Notices)
- Voluntary publication of Article IV consultation reports
- Increased contacts with broader set of economic stakeholders and local media

III. The Coverage of Surveillance in 2000-01

A. Introduction

64. As discussed in Chapter II, the framework of surveillance has evolved considerably over the years: coverage has expanded from an initial focus on exchange rate, monetary, and fiscal policies to structural policies, capital account developments and vulnerabilities, financial sector surveillance, and institutional issues; new tools have been developed to address these issues; and the modalities of surveillance have been adapted, particularly with a view to making surveillance more continuous, strengthening multilateral surveillance, and enhancing the integration of bilateral and multilateral surveillance.

65. At the same time, the Executive Board has repeatedly underscored the importance of keeping surveillance focused—a point that was also stressed by the external evaluators of surveillance.[28] At the discussion of the 2000 biennial surveillance review, Directors concluded that macroeconomic relevance remains a pertinent test for the inclusion of issues in Article IV reports. In addition, many Directors saw a hierarchy of concerns relevant for Fund surveillance. While placement of specific issues on this hierarchy could vary over time and from country to country, issues related to external sustainability and vulnerability to balance of payments or currency crises would be at the apex of this hierarchy.

66. Ensuring a proper focus on the most critical policy issues is, however, only one ingredient of effective surveillance. Equally important is that these issues are covered well, based on adequate expertise and information. Finally, the various elements covered in the surveillance exercise need to be integrated into a coherent overall assessment of a country's macroeconomic situation, crisis vulnerabilities, and the resulting policy challenges.

67. The broadened framework of surveillance has clearly complicated the task of accomplishing these objectives. Faced with a wider range of issues that are potentially relevant for the surveillance exercise, ensuring an appropriate focus of coverage has become more difficult. Focused surveillance does not mean limited monitoring: mission teams have to be aware of a broad range of issues while focusing discussions and reports on the most important ones. Inclusion of areas outside the Fund's traditional focus on macroeconomic issues has required new information and new expertise. And while the importance of covering issues such as financial and corporate sector vulnerabilities has become evident in recent crises, incorporating them into a coherent overall assessment has not always been straightforward.

68. This chapter examines how surveillance in 2000-01 has coped with these challenges. Specifically, based on a review of bilateral, regional and multilateral surveillance reports it addresses the following questions.

[28] *External Evaluation of Fund Surveillance,* IMF Website, September 14, 1999.

- Was the broadened framework of surveillance applied selectively but efficiently, taking due account of the key objectives of surveillance, the need for uniformity of treatment across the membership, and country-specific circumstances?

- How well were areas requiring special information and expertise covered?

- To what extent were the various elements of the surveillance exercise integrated into a coherent overall assessment?

B. Methodology

69. The analysis of the conduct of surveillance in 2000-01 is based on a review of Article IV consultation reports, complemented by a review of relevant reports on regional surveillance, as well as World Economic Outlook (WEO) and International Capital Markets (ICM) reports (Box 4).[29]

70. The sample of countries reviewed comprised approximately seventy countries from six country groups. Only non-program countries, i.e. members that did not have a Fund-supported program during the period from January 1, 2000 to December 1, 2001, or had "graduated" from a Fund-supported program during that period, were included.[30] The six country groups covered were: major advanced economies, other advanced economies, emerging-market economies, small developing countries, oil-exporting developing countries, and other developing countries.[31] The sample was roughly balanced between advanced, emerging-market, and developing economies (see Appendix Table 1).

[29] Specifically, the analysis was based on reports for the 2000 and 2001 Article IV consultations that were circulated to the Board by December 1, 2001, the 2000 and 2001 reports on the monetary and exchange rate policies of the euro area, the 2001 reports on the Eastern Caribbean Currency Union, and the 2000 and 2001 WEO and ICM reports.

[30] A country was considered to have graduated from a Fund program during the period from January 1, 2000 to December 1, 2001 if its program ended during that period and there was no discussion of a successor program. See the companion paper on *Surveillance in a Program Environment* for a discussion of surveillance in program countries.

[31] These country groupings were based on the WEO country classification, a GDP threshold (for the selection of small states), and the composition of the EMBI Global and MSCI indices (for the list of emerging-market economies). A separate grouping for transition countries was initially considered. However, the number of non-program, non-emerging-market transition countries proved too small.

Box 4. The Focus of the WEO and ICM Reports in 2000 and 2001

Over the past two years, the WEO reports have focused on the changing cyclical situation in the world economy against the background of increasing trade and financial linkages among countries and common global shocks. The role of international linkages and spillovers across countries from fluctuations in activity were extensively analyzed in the October 2001 WEO, with the conclusion that the rise in integration had indeed contributed to the synchronized global downturn. The global information technology revolution was highlighted as a key influence tying together recent business cycles across countries. Beyond integration among advanced economies, the impact on developing countries of developments in industrial countries was assessed, pointing to strong effects on Asian economies in particular. In this context, throughout WEO publications over the period considered, the impact of the deepening economic malaise in Japan on the rest of the world economy, and most importantly Asia, was extensively discussed. The policy requirements for the successful financial integration of developing countries into world capital markets were also analyzed.

The terrorist attacks on September 11, 2001, coming on top of the deepening global downturn, led to the publication of an interim WEO assessment in December 2001. This assessment dealt extensively with the channels through which the attacks would affect the global economy and the spillovers across economies and markets. The policy requirements and responsibilities of member countries for contributing to global recovery were outlined, against the background of the Managing Director’s statement to the Executive Board on the actions needed by member countries of October 5, 2001.

The WEO of May 2001 addressed the issue of fiscal policies in advanced economies, underscoring that policy challenges remained to ensure that the widespread improvement in fiscal positions in recent years was sustainable in light of changing cyclical positions and the future demand of population aging. The policy requirements for safeguarding inflation in emerging markets were also assessed, as were the factors leading to movements in major currency values, with a focus on the euro/dollar exchange rate. The focus of the October 2000 WEO was on global developments in equity markets and the associated policy challenges, as well as the experience of transition economies and the future policy agenda for ensuring further catch-up with advanced economies.

Against the backdrop of the sharp asset price surge and subsequent correction in mature and emerging markets, the 2000 and 2001 *International Capital Markets* reports analyzed capital markets developments and a number of special topics from a cross-country perspective. The 2000 report chronicled the run-up in asset prices, particularly in technology-related equities, and the subsequent sharp correction and its implication for financial stability. Intense competition spurred the development of new financial instruments and the use of these financial innovations to enter new markets. The report examined two aspects of this process of innovation and market penetration: the global over-the-counter derivatives market and the expansion of foreign-owned banks into emerging markets. Drawing on regular meetings with the private sector, the report also presented market participants’ assessments of proposals for private sector involvement in the prevention and resolution of crises. In the context of the 2001 WEMD, the capital markets team prepared a paper for Board discussion on the international financial market implications of the shrinking supply of U.S. Treasury securities. Later in the year, the 2001 ICMR report described how the global economic slowdown prompted a reappraisal of financial risk in a wide range of financial markets that also significantly affected private financing to emerging markets. Against this background, the report discussed, from a multilateral perspective, the financial implications and policy issues surrounding structural changes in the major government securities markets and the predominantly cross-border financial sector consolidation in emerging markets.

71. For each report, the treatment of macroeconomic policies (fiscal, monetary, and exchange rate policies), trade polices, capital account issues, external sustainability and vulnerability, financial sector issues, structural policies, institutional issues, and data issues was examined. In addition, the coverage of matters related to the overall functioning of the international financial system—hereafter referred to as systemic issues—was reviewed.

72. The rationale underlying this approach was to examine the focus of surveillance for groups of countries that share a number of important characteristics and, therefore, could be expected to share certain features in the coverage of surveillance. The objective was to identify both inter- and intra-group variations in the focus of surveillance, with a view to addressing the broad questions listed above.

C. Assessment of the Coverage of Surveillance in 2000-01

73. The results of the survey of bilateral and multilateral surveillance reports are summarized in Table 1. They offer the following conclusions.

Focus of Coverage

74. The focus of surveillance varies considerably across country groups: Fund surveillance is not a one-size-fits-all exercise. The broadened framework of surveillance appears to have helped draw attention to a wide range of issues that are potentially relevant, but it has been applied selectively. While the review does not allow judgment on the adequacy of the focus of surveillance in every individual case, it does suggest that much of the variation reflects differences in country-specific circumstances.

75. In major advanced economies, surveillance typically focused on cyclical developments, the stance of fiscal and monetary policies, the medium-term fiscal outlook, and structural policies needed to boost potential growth (e.g., labor market policies in continental European countries, financial and corporate sector restructuring in Japan) or to ensure medium-term fiscal sustainability in the face of aging populations (e.g., pension and health sector reforms). Substantial attention was devoted to the impact of economic conditions, prospects, and policies of the largest economies (the United States, the euro area, and Japan) on the global economy, and to the factors underlying the movements of the three major currencies (Box 5).

76. Surveillance in other advanced economies focused essentially on the same issues but, for good reasons, lacked the systemic dimension of surveillance in the large advanced economies. In addition, reports for non-euro-area members (e.g., Australia, New Zealand), contained substantial coverage of exchange rate movements, capital account developments, external vulnerabilities, and financial sector issues.

Table 1. Coverage of Surveillance, 2000-01					
Major Advanced Economies	***Other Advanced Economies***	***Emerging-Market Countries***	***Small Developing Countries***	***Oil-Exporting Countries***	***Other Developing Countries***
Macroeconomic Developments and Policies, and Exchange Rate Issues					
• Extensive coverage of cyclical developments, short-term outlook, short-term fiscal and monetary stances. • Medium-term fiscal sustainability addressed, particularly in continental Europe (Stability and Growth Pact (SGP)) and Japan (high level of public debt). • Substantial discussion of exchange rate developments, with particular emphasis on development of the US dollar, the euro, and the yen. • Focus on systemic implications of economic developments and policies.	• Extensive coverage of cyclical developments, short-term outlook, short-term fiscal and monetary stances, and medium-term fiscal sustainability. • Substantial discussions of exchange rate developments in countries with independent floats (Australia, New Zealand, Sweden, Switzerland).	• Substantial coverage of macroeconomic developments, monetary and fiscal policies. • Extensive discussion of the level of exchange rate and the adequacy of the exchange rate regime in countries with "soft" pegs. • Limited discussion of exchange rate issues in countries with floating exchange rates or currency boards.	• In most countries, focus on the consistency of macroeconomic policies with the pegged exchange rate regime and on medium-term fiscal sustainability. • In these countries, exchange rate regime generally not called into question. • In the few countries with an independently floating exchange rate regime, more detailed analysis of monetary policy and exchange rate developments.	• Discussions of macroeconomic policies dominated by fiscal policy focusing on the medium-term sustainability of the fiscal position, the level of public savings, and the insulation of the state budget from oil price fluctuations. • Limited discussions of monetary and exchange rate policies given long-standing pegged exchange rate regimes. • For countries with multiple exchange rates (Iran, Libya), substantial discussion of existing regime and strategies to achieve exchange rate unification.	• Discussions dominated by fiscal issues with emphasis on fiscal sustainability. • Coverage of exchange rate policies centered on exchange rate unification (in countries with multiple exchange rates), and external competitiveness (in countries with pegged exchange rates).
Structural Policies					
• Extensive coverage in continental Europe (labor market policies, health sector, and pension reforms) and Japan (corporate restructuring). • More limited coverage in Canada, the United Kingdom and the United States.	• Substantive coverage, focusing on policies to enhance growth and increase flexibility (labor and product market reforms) and to underpin medium-term fiscal sustainability (pension and health sector reforms).	• Variable coverage according to country specific circumstances (e.g., labor market reforms in countries with high unemployment, privatization in transition economies).	• Substantial coverage typically centered on reforms to ensure medium-term fiscal sustainability (e.g., civil service reform) and to structural policies to lift potential output growth and reduce vulnerability to shocks through greater diversification. • In a few cases, discussion of environmental issues.	• Discussions centered on reforms designated to improve the structure of public finances (e.g., development on non-oil-based revenue sources), and facilitate private sector led growth (e.g, foreign direct investment regime, labor market policies).	• Major element of surveillance over this group of countries • Variable focus, depending upon country-specific circumstances (e.g., exchange rate, price, and trade liberalization; reforms needed to ensure medium-term fiscal sustainability; policies needed to stimulate private-sector-led growth).

Table 1. Coverage of Surveillance, 2000-01

Major Advanced Economies	***Other Advanced Economies***	***Emerging-Market Countries***	***Small Developing Countries***	***Oil-Exporting Countries***	***Other Developing Countries***
Trade Policy					
• Substantial coverage for the United States, European Union, Japan and Canada. • Coverage of market access issues, including impact of agricultural and other subsidies, and use of antidumping measures.	• Substantial coverage of the trade policy regime for European Union members (in regional surveillance), and a few other countries.	• Light coverage in countries with liberal trade regime. • More thorough discussion of existing restrictions in other countries, with focus on tariffs.	• Coverage generally limited to information on tariffs and non-tariff barriers. • Generally, limited discussion of trade policy reforms, including in countries with substantial trade barriers.	• In countries with relatively restricted regimes (Libya, Iran), substantial coverage of recent policy changes and plans for future trade reform. • Limited coverage in other countries.	• Variable coverage, with focus on tariffs and non-tariff barriers. • Limited discussion of specific trade liberalization measures. • Occasional references to regional trade arrangements.
Financial Sector Issues					
• Substantial coverage for Japan, both in bilateral and multilateral reports. • For other countries, coverage limited to description of recent initiatives.	• Generally, brief coverage for euro-area countries, except for countries having participated in the FSAP (e.g., Finland, Ireland). • Substantial analysis of financial sector health for Australia and New Zealand.	• Substantial coverage in all countries, with variable focus. • Emphasis on existing vulnerabilities and policies to reduce these vulnerabilities in Asia, and, to a lesser extent, Latin America. • Focus on development issues in Central and Eastern Europe. • Deeper coverage in countries that participated in the FSAP and countries that experienced a financial sector crisis.	• Coverage in all staff reports. • Analysis of on-shore financial sector generally confined to a general statement about the soundness of the banking sector . • Substantial attention to off-shore financial center activities, including factual information on action to improve supervision of OFC activities and strengthen anti-money-laundering efforts.	• Coverage in all staff reports. • Detailed coverage of financial sector developments, vulnerabilities and policy recommendations for countries that participated in the FSAP.	• Variable coverage. • Detailed and candid assessments of the financial sector and related vulnerabilities for countries having benefited from a FSAP. • For other countries, little or no discussion of financial issues, except for a few cases.

Table 1. Coverage of Surveillance, 2000-01

Major Advanced Economies	***Other Advanced Economies***	***Emerging-Market Countries***	***Small Developing Countries***	***Oil-Exporting Countries***	***Other Developing Countries***
Capital Account Developments; External Sustainability and Vulnerability					
• Discussions of capital account developments in the context of analysis of exchange rate developments.	• Substantial treatment of capital account development as well as financial and external sector vulnerabilities for Australia and New Zealand. • Brief coverage for most other countries.	• Key elements of surveillance in all countries. • External vulnerability assessments as the basis for the analysis of macroeconomic policies and structural reforms in several countries (e.g., China, Lebanon, Korea, Philippines, Thailand and Malaysia). • In other countries, focus on a few key issues (e.g., impact of the macroeconomic policy mix on capital inflows, the exchange rate level and the current account deficit in central European countries). • Discussion of the medium-term sustainability limited to a baseline scenario, with little or no coverage of upside and downside risks.	• Generally, brief coverage of capital account developments, given limited access to international capital markets. • Discussion of the medium-term sustainability limited to a baseline scenario, with little or no coverage of upside and downside risks.	• Focus on the medium-term sustainability of the current account and the impact of oil price fluctuations, fiscal policy and structural reforms on the external position.	• Discussions centered on current account developments (e.g. fluctuations in commodity prices) and policy implementation. • Extremely limited coverage of capital account issues given lack of market access and highly regulated capital account.
Institutional Issues					
• Selective treatment, focusing on areas closely linked to key policy issues (e.g., medium-term fiscal framework in the euro area, fiscal and monetary policy transparency in Japan).	• Selective coverage (e.g. monetary policy framework on Australia and New Zealand, wage-setting framework on Iceland).	• Selective coverage (e.g., corporate governance and insolvency regime in Asia, governance and transparency in Russia).	• Coverage generally limited to financial supervision of on-shore and off-shore financial sectors.	• Coverage of mechanisms to insulate domestic macroeconomic developments from oil price fluctuations (e.g., oil stabilization funds). • Attention to fiscal transparency (treatment of oil revenues).	• Selective coverage.

Table 1. Coverage of Surveillance, 2000-01					
Major Advanced Economies	***Other Advanced Economies***	***Emerging-Market Countries***	***Small Developing Countries***	***Oil-Exporting Countries***	***Other Developing Countries***
Data Issues					
• Succinct treatment.	• Succinct treatment.	• Variable treatment with substantial coverage in countries perceived to suffer from major statistical weaknesses.	• Variable coverage.	• Substantial coverage of data issues, focusing on provision of fiscal, reserves, and foreign asset data.	• Coverage focusing on adequacy of data provision for effective surveillance and actions to remedy existing statistical weaknesses.
Systemic Issues					
• Brief coverage of anti-money-laundering efforts, initiatives to combat bribery, and level of official development assistance.	• Brief references to the level of official development assistance and, in some cases, anti-money-laundering efforts and initiatives to combat bribery.	• Coverage limited to factual descriptions of anti-money-laundering efforts in countries included on past or present FATF lists.	• Little or no coverage.	• Little or no coverage.	• Little or no coverage.

Box 5. Coverage of the Systemic Impact of Policies in Major Advanced Economies

In the context of the synchronized nature of the global economic slowdown in 2001, the systemic impact of economic policies in the United States, the euro area, and Japan—hereinafter referred to as G-3—represented a central focus of the IMF's multilateral surveillance and an important element of bilateral surveillance.

The regular WEO reports in May and October 2001 and the interim report in December 2001 shared a common emphasis on global challenges and systemic implications of economic policies of the G-3 countries. Against the background of marked slowdown in the United States, stalling recovery in Japan and moderating growth in Europe, the May 2001 report underlined the rapid response of policy makers led by the US Federal Reserve. The report emphasized the importance of monetary easing to support economic activity and reduce international spillover effects of the slowdown. It also analyzed the risks and implications of foreign exchange developments in the G-3 countries, in particular the appreciation of the US dollar and corresponding weakening of the euro. As global economic conditions worsened, the October 2001 report thoroughly examined the international business cycle linkages among G-3 economies as well as between advanced and developing economies. Noting the increasing global integration and interdependence of business cycles, the report stressed, throughout the Fund membership, prudent policymaking requiring the monitoring and assessment of macroeconomic developments and policies abroad. The December 2001 interim WEO report called for a coordinated and collaborative policy response by G-3 countries to sustain demand through further monetary policy easing if necessary, especially in Japan, and appropriate fiscal action.

Also in the context of multilateral surveillance, the August 2001 ICM report examined the systemic impact of financial developments in mature markets, especially the United States, on the global financial system. In particular, the analysis stressed the main risks facing international financial markets stemming from a possible further repricing in US and global equity and fixed-income markets, a potential disruptive drop in the value of the dollar, and the financial market fallout of an unwinding of the US domestic and external financial imbalances. The report also examined the vulnerabilities of the Japanese banking system, including the risks associated to a correction of compressed yields in the Japanese government bond market, and considered the euro area's vulnerabilities to contagion and spillover effects from a potential deterioration in financial conditions in the United States. In addition, it emphasized recent developments on structural issues adding to the complex dynamics of international financial transactions and transmission channels of financial shocks.

The 2001 Article IV consultation reports for the United States, euro area countries and Japan also examined the systemic implications of exchange rate and monetary policies emphasizing traditional transmission mechanisms through trade, financial and monetary linkages. Reflecting the prominent role of its economy, the report for the United States analyzed the various channels through which the US economic slowdown and the ensuing policy response could affect the global economy. This analysis also highlighted the global risks of a potential sharp depreciation of the dollar and a disorderly adjustment of the current account. The report for Japan, while supportive of a more aggressive monetary policy easing, considered the impact of the yen depreciation on Asian economies, noting that the consequences for the region of a weaker yen would be more manageable than during the Asia crisis, given the adoption of more flexible exchange rate regimes in many countries and their healthier external debt profiles. The report for the euro area underscored the limited impact of monetary policy to prevent the slide in the euro and the associated capital account developments, which were seen to have been largely driven by factors such as portfolio diversification and expectations of increased US productivity growth over the medium term. Moreover, the reports for France, Germany and Italy recommended giving full play to fiscal automatic stabilizers in 2001 to sustain demand and prevent further deterioration of global economic conditions.

77. In emerging market economies, vulnerabilities to both domestic and external crises, including those related to capital account developments, financial sector problems and weaknesses in the corporate sector, were at the center of surveillance, together with macroeconomic, structural, or institutional policies needed to minimize identified vulnerabilities. In particular, in several Article IV consultation reports for emerging market countries—especially but not exclusively those for countries affected by the Asian crisis—key vulnerability assessments served as the organizing principles for discussions of macroeconomic policies, structural reforms, and institutional reforms.

78. In small developing countries, which predominantly maintain pegged exchange rate regimes, are dependent on exports of a few goods or services, and have little or no access to international capital markets, surveillance typically focused on three areas: the consistency of short-term fiscal and monetary policies with the fixed exchange rate regime, reforms needed to ensure medium-term fiscal sustainability (e.g., civil service reform), and structural policies designed to lift potential output growth and reduce vulnerability to shocks through greater diversification.

79. In oil-exporting countries, reducing macroeconomic vulnerability to oil price fluctuations, ensuring an optimal use of proceeds from nonrenewable resources, and promoting the development of the non-oil sector were the key issues addressed in surveillance. Thus, Article IV consultation reports generally focused on fiscal issues such as the level of public savings, the budget structure (e.g., containment of current expenditures, development of non-oil-based sources of taxation), mechanisms to insulate the state budget from oil price swings (e.g., oil stabilization funds), as well as policies to facilitate private-sector-led growth (e.g., liberalization of foreign direct investment, promotion of a competitive market environment, liberalization of the financial sector).

80. The focus of surveillance in other developing countries varied widely, given the diversity of the sample. In some countries, Article IV consultations gave particular prominence to exchange rate, price, and trade liberalization as the main economic challenge was to move toward market-oriented policies. In another group, fiscal consolidation and public finance reform dominated the discussions. In a third group, fiscal policies and structural reforms (including public sector reform, financial sector reform, and trade policies) to generate higher growth and promote poverty alleviation were given center stage. In these countries, as in most other developing countries, macroeconomic and structural policy issues were typically closely linked and it was frequently difficult to separate the two.

Depth of Coverage

81. While the range of issues covered in surveillance has expanded substantially, macroeconomic developments and policies have remained at the center of surveillance activities in all countries. Focus and perspective of coverage have varied considerably across countries—ranging from cyclical conditions in industrial countries to medium-term fiscal sustainability in oil exporting countries and growth prospects in low-income developing

countries. The analysis has typically been well founded and integrated, reflecting the long-standing expertise of Fund staff in this area.

82. Exchange rate issues have been at the heart of the Fund's surveillance from its inception and were discussed in all reports, albeit to a varying degree. Greater skepticism on the durability of "soft pegs"—or closely related regimes (e.g., narrow bands)—in countries with market access has prompted candid discussions on the sustainability of such exchange rate regimes in emerging market countries (Box 6). Conversely, other exchange rate regimes in emerging market countries, including currency boards, have generally not been questioned. The exchange rate pegs prevailing in most small developing and oil exporting countries have rarely been the subject of extensive discussions either. In these countries, with the noteworthy exception of those maintaining complex, multiple exchange rate regimes, surveillance has generally focused on the consistency of macroeconomic policies with the existing exchange rate regime. The regime itself and the current level of the peg were usually not called into question, except when developments (e.g., depletion of reserves, external arrears, intensification of exchange rate restrictions) pointed to large and pressing external imbalances. This limited coverage may be related to perception that candid treatment of these issues in staff reports could trigger adverse market reactions. For countries with flexible exchange rate regimes, discussions have tended to focus on exchange rate movements, their possible causes and the potential reversal. However, the depth of the underlying analysis has varied, with analyses relying on more sophisticated quantitative tools typically limited to the advanced economies.

83. Coverage of structural issues has been selective and the focus has, consequently, varied widely according to country-specific circumstances. Nevertheless, certain areas of structural reform—notably reforms to strengthen public sector finances—have prominently featured in surveillance exercises with many different economies, advanced as well as developing ones. While the macroeconomic rationale for covering certain structural issues is typically evident, the intensity of the linkages between macroeconomic and structural policy issues clearly varies across countries. In many developing and transition economies, macroeconomic and structural policies often seem inextricably linked. Given widespread structural rigidities and distortions in these countries, it appears difficult to conceive of a meaningful discussion of macroeconomic policies that ignores the structural aspects of fiscal sustainability, external viability, and sustainable growth. Indeed, in some instances, issues such as the implications of the AIDS epidemic may be crucial for the assessment of macroeconomic prospects.

Box 6. Coverage of Exchange Rate Issues in Hungary and Malaysia

At the time of the latest Article IV consultations, Hungary and Malaysia maintained respectively a narrow band exchange regime and a fixed exchange rate.

Hungary

The 2000 Article IV Consultation report for Hungary contained an extensive discussion of the monetary framework and the exchange rate regime, as well as a detailed analysis of external competitiveness.

The report indicated that (i) there was broad agreement between the staff and the authorities that the narrow band exchange regime had been instrumental in supporting Hungary’s successes; (ii) in a setting characterized by the absence of heavy capital inflows, foreign trading on the strong side of the band, and a healthy current account position, the authorities recognized that a more flexible exchange rate regime would provide more scope for monetary policy to react to inflationary developments; (iii) staff strongly supported a move to a more flexible exchange regime and argued for an early move, noting that increased exchange rate flexibility would allow the central bank more leeway to respond to demand pressures, discourage unhedged borrowing by corporations, and make a resumption of strong interest-rate sensitive capital inflows less likely by raising the exchange risk premium. On the basis of a variety of indicators and cross-country analysis, the report concluded that Hungary’s export competitiveness was strong.

In the event, the authorities widened the exchange rate on May 4, 2001. At the conclusion of the 2000 Article IV Consultation, Executive Directors welcomed the widening of the exchange rate band (PIN No. 01/47, 5/18/2001).

Malaysia

The 2001 Article IV Consultation report for Malaysia included an wide-ranging discussion of the exchange rate regime and the consistency between the exchange rate peg and macroeconomic policies.

The report emphasized that (i) the authorities had reiterated their intention to maintain the peg, arguing that the ringgit was not misaligned; (ii) monetary policy in the coming year would be geared to support economic growth; (iii) the staff observed that the combination of an exchange rate peg with low interest rates and an expansionary fiscal policy could become inconsistent; (iv) the staff expressed serious concern about the prospect of substantial short-term capital outflows; (v) while agreeing that the recent decline in reserves was a matter of concern, the authorities noted that special, nonrecurring factors had contributed to accelerated capital outflows; and (vi) staff was of the view that the authorities should stand ready to adjust macroeconomic policies as necessary to defend the peg, if they were convinced that a move in the exchange rate regime was imprudent under current conditions.

At the conclusion of the 2001 Article IV Consultation, Executive Directors noted that, under certain circumstances, the pressure on the ringgit could be renewed, and that, should such an eventuality materialize, there would likely be a need to reassess the consistency between the macroeconomic policy stance and the exchange rate regime (PIN No. 01/114, 11/2/2001). A few Directors suggested that the authorities consider introducing greater flexibility in the exchange rate regime; and all Directors agreed that the timing of such a move was an important issue, noting that any shift in the exchange regime at the prevailing highly uncertain global economic outlook and unsettled international financial markets could be destabilizing.

84. While, in most instances, the macroeconomic relevance of the structural policy issues covered in the context of surveillance is clear, the depth of coverage of these issues is not always consistent. In certain instances, particularly on topics related to the Fund's traditional areas of expertise, discussions of structural issues are substantial. In certain other instances, they lack specificity or appear limited to a repetition of past recommendations. In the latter cases, coverage might be improved by drawing more on the expertise of other institutions, as recommended by the Executive Board at the conclusion of the 2000 biennial review of surveillance. Currently, explicit references to work done by other institutions are relatively rare in Article IV consultation reports, with some exceptions (e.g., OECD studies on labor market policies).

85. Trade policy has been addressed in all Article IV consultations, but the depth of coverage has varied widely. Trade policy issues received substantial attention in reports for major advanced economies (the United States, the euro area/European Union, Japan, and Canada), which stressed, inter alia, the need to roll back agricultural and other subsidies and improve market access for developing countries. In other countries, coverage of trade issues has varied, sometimes but not always in line with the restrictiveness of the trade regime. In addition, multilateral trade issues have been the subject of substantial coverage in WEO reports.[32]

86. While financial sector surveillance has become a standard element of Fund surveillance, coverage has shown substantial variation. To an extent, this is justified by differences in the development of the financial sector, access to external finance, and, generally speaking, potential interactions between macroeconomic and financial sector developments. However, differences in coverage of financial sector issues also reflect resources and expertise brought to bear on the analysis of these issues. Participation in the FSAP has generally enriched the treatment of financial sector issues in a very substantial manner. The benefits of FSAP participation have included greater availability of data (e.g., financial soundness indicators), better ability to assess the fragility (or strength) of the financial sector and quantify the impact of macroeconomic shocks (e.g., lower growth, sharp exchange rate depreciation, an interest rate spike) on the financial system, and the ability to analyze in greater depth the potential impact of a financial sector crisis on macroeconomic developments (e.g., fiscal costs of banking sector restructuring). Altogether, participation in the FSAP, combined with close integration of the FSAP work in the Article IV consultation process—though not a panacea—allows a more substantial discussion of potential problems and possible remedies to existing financial sector weaknesses (Box 7). In countries that did not participate in the FSAP, a similar depth of coverage of financial sector issues could generally only be found in cases where a financial sector crisis had occurred—and, thus, considerable technical work had been done by the Fund, the World Bank, and other institutions—or where the existence of important financial sector weaknesses had been established for some years. In many other countries, the treatment of conditions in the financial sector has been relatively limited, mostly due to lack of adequate information.

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[32] See, for instance, *"The World Trading System: From Seattle to Doha", World Economic Outlook,* September 2001; and *"Trade Integration and Sub-Saharan Africa," World Economic Outlook,* March 2001.

Box 7. Iceland—Fund Surveillance in 1999-2001[1]

Iceland was placed on the 24-month consultation cycle in December 1997.

In May 1999, at the conclusion of the 1999 Article IV Consultation, the Executive Board noted that Iceland was beginning to overheat and that the key challenge for economic policy was therefore to safeguard the hard-won record of low inflation and financial stability. Executive Directors stressed that the strong economic upswing in Iceland had been accompanied by a rapid increase in bank lending facilitated by capital account liberalization and financial deregulation in the mid 1990s, and a substantial rise in the household and corporate sectors' indebtedness.

Iceland volunteered for participation in the Financial Stability Assessment Program (FSAP); and, in November 2000, an FSAP mission visited Iceland. The mission found that both macroprudential and microprudential indicators suggested that the financial system might be vulnerable to a macroeconomic shock. It noted that the legislative framework was in broad conformity with the major supervisory standards, but observed that some shortcomings in the regulatory and supervisory framework as well a number of institutional features might give rise to systemic instability. At the same time, the mission recognized that the financial sector was dynamic, appropriately responding to regulatory reform and market signals, and that there was competence in prudential oversight. Thus, it concluded that the authorities appeared to be in a relatively strong position to address existing vulnerabilities.

In January 2001, an Article IV consultation mission went to Reykjavik. The mission confirmed that domestic (e.g., excessive domestic credit and demand growth) and external (e.g., a widening current account deficit, a surge in foreign borrowing by banks) imbalances were a cause of significant concern. It pointed to the need to lower the risk exposure of the financial system. It supported plans under consideration to abandon the "soft" exchange rate peg in favor of a float, accompanied by inflation targeting, and called for fiscal policies supportive of the new monetary policy framework.

In March 2001, the Icelandic authorities announced the abandonment of the exchange rate band and the shift to inflation targeting.

In May 2001, the Executive Board concluded the 2001 Article IV consultation with Iceland. Directors noted the sustained overheating of the economy and the deterioration in some macroprudential indicators. They welcomed the decision to allow the currency to float. Pointing to the timeliness of Iceland's participation in the FSAP, they stressed the need to lower the risk exposure of the financial system. Against this background, Directors recommended that Iceland be moved temporarily to a 12 month consultation cycle.

The above experience suggests that Iceland's participation in the FSAP enhanced the quality of Fund surveillance in 2001, by increasing its focus on financial sector vulnerabilities and potential links between macroeconomic and financial sector developments.

[1]See *IMF Concludes Article IV Consultation with Iceland* (IMF website, PIN No. 99/42, 5/20/1999); *Iceland—Financial System Stability Assessment* (IMF website, 6/12/2001); *Iceland—2001 Article IV Consultation—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Authorities of Iceland* (IMF website, 6/12/2001)

87. The coverage of capital account developments and discussions of various aspects of a member's vulnerability to a currency crisis have been most prominent and explicit in the emerging market countries and a few advanced economies (New Zealand, Australia). In developing countries without market access, vulnerability assessments have typically been subsumed in discussions on the current account outlook and the consistency of macroeconomic policies with the exchange rate regime. However, coverage of crisis vulnerabilities has also varied within the group of emerging market countries, with more extensive treatment observed in Asia. In this region, vulnerability analyses have tended to employ a variety of indicators, including indicators of financial and corporate sectors' exposure to exchange and interest rate risks; in other countries, use of vulnerability indicators has often been more limited, although short-term debt to reserves ratios and other debt- and reserve-related indicators have been commonly reported.

88. Even in countries with relatively extensive coverage of crisis vulnerabilities, one weak link in the analysis has commonly been the assessment of medium-term debt sustainability. While nearly all Article IV consultations reports for emerging market and developing countries contain a medium-term balance of payments scenario—a legacy of earlier efforts to address debt sustainability issues in the wake of the 1980s debt crisis—the usefulness of these scenarios for a meaningful analysis of debt sustainability is often questionable. In most cases, the medium-term balance of payments analysis is limited to the presentation of a baseline scenario with optimistic assumptions on growth, interest, and exchange rates and little or no substantial discussion of risks or alternatives.

89. Institutional issues—ranging from inadequate bankruptcy laws to fiscal policy frameworks—have typically been covered selectively, according to country-specific circumstances. As in the case of financial sector surveillance, coverage of issues related to the institutional features of an economy frequently requires special expertise that goes beyond the Fund's traditional focus on macroeconomics. In a number of cases, ROSCs have helped strengthen the coverage of institutional issues, by providing a consistent framework to assess observance of a standard or code, recognize existing institutional strengths, and identify weaknesses as well as potential remedies (Box 8). In other instances, the contribution of ROSCs to the treatment of institutional issues appeared more limited. This might be explained by three factors: (i) on issues closely related to the Fund's traditional areas of expertise, (e.g., fiscal transparency, monetary transparency, statistical issues), the supplementary contribution of ROSCs to Fund staff's knowledge may not be explicitly attributed; (ii) some prepared ROSCs modules may relate to institutional issues that are not seen to deserve priority attention in surveillance—given their nature, ROSC may be prepared whether concerns exist about the related institutional issue or not; and (iii), possibly most importantly, for the period covered by this survey, very few ROSCs were prepared in institutional areas where Fund staff are likely to be most in need of other institutions' expertise (e.g., corporate governance, insolvency regimes). In the absence of ROSCs, the quality of coverage of institutional issues appears to have varied considerably, depending on whether the issues covered are closely related to the Fund's traditional areas of expertise.

Box 8. Use of ROSC Modules on Fiscal Transparency in Surveillance

ROSC modules on fiscal transparency and Article IV consultation reports for 12 countries were reviewed to assess whether, and how, these ROSCs had contributed to the coverage of fiscal transparency—an institutional issue—in bilateral surveillance. The randomly selected sample of countries included Argentina, Australia, Azerbaijan, Brazil, Bulgaria, Cameroon, Czech Republic, Estonia, Hungary, Pakistan, Turkey and Uruguay.

The main conclusions of this selective review of ROSCS are:

- ROSC modules were generally helpful in informing IMF surveillance (and program design). In most cases, ROSC modules provided both an assessment of weaknesses (and strengths) in fiscal transparency and specific recommendations to address these weaknesses.

- The degree to which ROSC assessments of fiscal transparency fed into surveillance reports varied across countries:

  In a number of cases (*Argentina*, *Azerbaijan*, the *Czech Republic*), staff reports contained a detailed discussion of the progress that the authorities had made in implementing the ROSC recommendations. In some of these cases, this discussion was facilitated by the preparation of a ROSC update.

  In other cases, coverage was more succinct. For instance, some reports indicated that staff had followed upon on the recommendations of the ROSCs but contained limited information on the contents of these discussions.

  In program countries, ROSC assessments were often discussed in program documents. For some of these countries, follow-up actions were described in the authorities' letters of intent.

- In general, Article IV consultation reports did not provide information on the timeframe for implementation of measures to correct weaknesses identified in ROSC modules, which, on occasion, made the assessment of progress more difficult.

These conclusions suggest that preparation of ROSC modules on fiscal transparency can help deepen the coverage of that issue in Fund surveillance; that ROSC modules are most useful for surveillance when they contain candid assessments and specific recommendations; and that, in certain cases, further efforts to translate ROSC module assessments into well-prioritized, specific action plans might be worthwhile.

90. Given the importance of adequate data for the quality of Fund surveillance, data adequacy has become a standard element of consultation discussions. Consequently staff reports have routinely covered data issues, even though the extent of coverage has naturally varied according to the quality of data available in a specific country.

91. Coverage of certain systemic issues—such as the implementation of the OECD Anti-Foreign Bribery Initiative or anti-money laundering efforts, has been mandated by the Executive Board, given the broad interest of the membership in these matters. Coverage of these issues in Article IV consultation reports is usually very brief (typically, a few sentences).

Integration of Coverage

92. The preceding review suggests that Fund surveillance has fully embraced the broadened framework, while applying it selectively according to country-specific circumstances. However, covering the various elements of the broadened framework does not automatically amount to a well integrated assessment of a country's macroeconomic conditions, vulnerabilities, and policy challenges. Proper integration of these elements would seem essential if the broadened framework is to strengthen surveillance. Thus, an important question is whether this integration has been achieved. In particular, can it be said that, where relevant, attention to global economic and financial developments, analysis of financial and external vulnerabilities, and coverage of such issues as corporate governance have been fully integrated with the "traditional" coverage of macroeconomic and structural policies to form a unified view of a given country's key policy challenges and possible actions to address these challenges?

93. While it is difficult to answer this question conclusively, the review of surveillance reports suggests that in many countries, this integration has not yet been fully achieved. In particular, in a significant number of countries, coverage of financial sector issues is largely an add-on to a well integrated macroeconomic analysis. Inadequate information in the absence of FSAP participation may account for this shortcoming. In 2000-01, FSAPs have been completed for only 14 percent of the Fund's membership. Vulnerability assessments were also not always fully integrated into the broader analysis. However, in several reports for emerging market countries, the various components of surveillance did add up to a unified, coherent exercise. Indeed, as noted above, in some of these reports, the discussions of external vulnerabilities—including the vulnerabilities of the financial and corporate sectors—served as the point of entry to the analysis of macroeconomic policies as well as structural and institutional reforms. This was the case in China (with a strong focus on financial and corporate sector vulnerabilities), Lebanon, and, in particular, the countries affected by the Asian crisis (Box 9). Reports for some developing countries without market access also added up to a unified, coherent exercise (Box 10).

Box 9. Coverage of External Vulnerabilities in Countries with Market Access: The Philippines

The staff report for the 2000 Article IV consultation for the Philippines is a good example of a report that well integrates the vulnerability analysis within the overall macroeconomic picture. The report does not discuss vulnerability as a separate issue; instead, it treats as an integral part of the policy framework.

The Article IV consultations were held in the midst of severe political turmoil that had a significant impact on financial markets.[1] In early October, a political crisis arising from allegations of corruption against President Estrada led to significant pressure on the peso, prompting sizeable foreign exchange intervention by the BSP and an increase in policy interest rates by 400 basis points.

In this setting, the Article IV discussions focused on how economic policy could help contain the fallout from the political crisis and contribute to turning around investor confidence. The report argued that reviving confidence would require—besides resolution of the political crisis—a credible start to fiscal consolidation, clear focus of monetary policy on containing inflation, continued structural reforms, and decisive steps to improve governance.

In light of the risks caused by the political turmoil, worries on vulnerabilities in the fiscal, banking, and external sectors were a recurring theme in the report:

- The report worried most about risks posed by fiscal policy. It pointed to the chronic weakness of national government revenues and high public debt (90 percent of GNP), which constrained the scope for expansionary fiscal policy in response to an adverse shock, and was a potential source of financial instability.

- The report also worried about increased vulnerabilities in the banking system. While it acknowledged that overall the banking system appeared fairly stable, it noted that there had been an increase in nonperforming loans, while recent episodes of deposit withdrawals from several banks indicated some fragility of deposit confidence in weaker banks.

- On the external sector, the report argued that while vulnerabilities had declined considerably in the past decade, risks persisted. The report pointed in particular to the increase in external debt, the reserve coverage that was less than other countries in the region, the sizeable capital outflows in 1999-2000, and the heavy concentration of export growth in electronics, which made the country vulnerable to sudden shifts in demand.

Policy discussions on vulnerability were interwoven with discussions on the medium-term strategy to achieve sustained high growth and reduce poverty. According to the report there was no clear-cut division between policy reforms that would reduce vulnerability and policy reforms that would enhance growth perspectives; rather, most policy reforms would do both. For example, a reduction of fiscal deficits would both reduce vulnerability and increase private investment and growth; while reforms of the banking system would both make it less vulnerable to a crisis and build a more efficient banking system.

[1] The Article IV discussions took place during October 6-18 and December 6-13, 2000.

Box 10. Coverage of External Vulnerabilities in Countries without Market Access: The Seychelles

After rising by 5 percent during the previous two years, the Seychelles' real GDP stagnated in 1998-99 with serious current account difficulties threatening its external sustainability. The underlying macroeconomic imbalance causing these difficulties was the Seychelles' large fiscal deficit, which doubled from about 7 percent of GDP during 1993-95 to 14 percent during 1996-99, resulting from a surge in capital outlays and net lending as well as a steady growth in current spending. With insufficient autonomous capital inflows to finance these larger deficits, a policy of accommodating large budget deficits by a substantial easing of monetary conditions (broad money increasing by 19 percent per year during 1995-1999), and maintenance of the official exchange rate unchanged, the external current account deficit widened to 17 percent of GDP by 1999, international reserves dropped to less than 2 weeks of imports, external payments arrears accumulated, and foreign restrictions were tightened. The demand for foreign exchange, especially from sectors without preferential access to foreign exchange, spilled over into the parallel foreign exchange market, where the premium reached up to 100 percent.

In light of the above developments, the 2000 Article IV consultation with the Seychelles and the resulting staff report focused squarely on the country's current account difficulties and its underlying fiscal imbalance bringing out the required policy adjustments in all key areas: exchange rate, fiscal, monetary and structural policies. The staff stressed the need for large fiscal consolidation along with structural measures to increase efficiency in the tax system, monetary policy restraint, a rapid correction in the misalignment of the official rate and movement toward greater exchange rate flexibility, and removal of distortionary exchange and price restrictions. Similarly, the Executive Board emphasized the need for improving public finances, realigning the exchange rate, tightening monetary policy, and removing administrative controls.[1] More specifically, the Board advised the authorities to target a surplus in recurrent fiscal operations and limit capital spending to an amount that could be covered by the recurrent surplus and foreign financing, including grants. The Board also stressed the need to correct the misalignment by unifying the official and parallel-market exchange rates and adopt sufficiently tight financial policies to pave the way for, and support action on, the exchange rate.

[1] See *IMF Concludes Article IV Consultation with Seychelles*, PIN No. 00/111, 12/26/2000.

D. Conclusions

94. Fund surveillance has embraced the broadened framework and has incorporated the lessons from the crises that prompted its evolution. Application of the framework has generally been selective with surveillance focusing on the issues that matter most for macroeconomic stability, external viability and growth in the specific circumstances of individual countries. This general conclusion extends to the coverage of structural policy issues, which has typically been appropriately selective and motivated by specific macroeconomic concerns, even though the quality of coverage could be strengthened by greater reliance on expertise from other institutions.

95. This said, there is, nevertheless, scope for strengthening the focus of surveillance. In particular, some areas are covered routinely in nearly all reports, but in many cases the treatment is very brief, largely because these issues are not seen as critical for surveillance in these countries. Coverage of trade policy is a case in point: while coverage of trade issues—including market access—for the United States, the European Union, Japan, and Canada was strengthened over the past two years, treatment of these issues in many other Article IV consultation reports appear routine. Greater selectivity in covering trade issues—concentrating on countries with serious distortions and systemic trade issues of market access—may be worth considering. Combined with greater depth and quality of coverage, buttressed by greater reliance on the technical expertise of other institutions, a more selective approach to the treatment of trade issues in bilateral surveillance could simultaneously strengthen the overall coverage of these issues and the focus of surveillance. This approach could be complemented by enhanced coverage of global trade issues in multilateral surveillance.

96. Another example of regular, but succinct, treatment is the coverage of systemic initiatives, such as efforts to combat money laundering, or the OECD Anti-Foreign Bribery Initiative. While it might be argued that the Article IV process—which is the most regular formal mode of interaction between the Fund and national authorities—is a convenient channel to address issues of broad interest to the membership as a whole, this consideration must be weighed against the danger of overloading the Article IV process and diluting its focus.

97. While the broadened framework of surveillance has helped draw attention to a range of “new” issues that have turned out to be critical for the effectiveness of surveillance in many countries, adequate treatment of these issues has frequently been constrained by limited information, expertise, or resources. This has been particularly evident in the coverage of financial sector issues, which has varied enormously, depending on the resources and expertise devoted to the exercise. The experience in the past two years suggests that an adequate depth of treatment of financial sector vulnerabilities is generally not possible solely with the staff resources devoted to regular Article IV consultations. Indeed, it was rarely achieved without the in-depth analysis afforded by prior participation in the FSAP. This raises important questions about the resource implications of financial sector surveillance and, given constraints on the number of FSAPs that can be concluded in a given year,

possible modalities for keeping financial system stability assessments derived from FSAPs up-to-date, and strengthening financial sector surveillance in the absence of FSAPs. If financial sector surveillance is to be treated as part of the core of the Fund's surveillance activities, the quality of treatment has to measure up to the quality of coverage of other core areas, notably macroeconomic policies and exchange rate issues.

98. The coverage of institutional issues in the context of Fund surveillance raises similar, albeit possibly not as pressing, questions as financial sector surveillance. Lack of adequate expertise and information often constrain the quality of coverage, especially on issues not closely related to the Fund's traditional areas of expertise. Work on ROSCs in areas such as fiscal transparency, monetary transparency, and data provision have often provided useful background information for surveillance discussions. However, in areas where the need for outside expertise is particularly pressing (e.g., corporate governance, insolvency regimes), preparation of ROSCs had lagged. Thus, in key institutional areas for certain countries, surveillance has yet to benefit fully from the work on standards and codes, and modalities for bringing the necessary expertise to surveillance in the absence of a ROSC may need to be considered.

99. While the assessment of vulnerabilities to a currency crisis has been quite comprehensive in several emerging market and advanced economies, data limitations have been a serious impediment in many countries. To be sure, given the dominant role of private capital flows in countries with market access, the data requirements for vulnerability assessments in these countries go well beyond the traditional requirements for Fund surveillance. In particular, information on private sector debt profiles and balance sheet exposure to exchange rate and interest rate risk is typically needed to assess fully vulnerabilities to changes in market conditions and exchange rates. Data on the nonfinancial corporate sector have been particularly scant; yet, as shown in recent emerging market crises, the assessment of financial sector vulnerabilities remains incomplete without adequate data on the nonfinancial corporate sector.[33]

100. Besides data constraints, a weak element of most vulnerability assessments and of surveillance more generally, has been inadequate coverage of medium-term debt sustainability issues. The medium-term balance of payments scenarios introduced in the wake of the 1980s debt crisis have largely become token exercises with little or no attention to the sensitivity of the projections to exchange rate or interest rate movements, or alternative growth assumptions. Greater attention to debt sustainability issues is likely needed to strengthen vulnerability assessments, not only in emerging market countries but also in countries relying primarily on official financing.

[33] The recent publication of *External Debt Statistics: Guide for Compilers and Users*, produced under the auspices of the Inter-Agency Task Force on Finance Statistics could facilitate compilation and dissemination of data on non-financial corporate external debt.

101. Besides better information and greater expertise, the quality of surveillance might be enhanced by greater candor in the coverage of key issues, particularly on exchange rate policies. While, in emerging market countries with "soft" pegs, the discussion of these issues has become more candid, which has appreciably strengthened the quality of coverage, existing exchange rate arrangements are typically not questioned in most other circumstances. In some of these cases, but not necessarily in all, this absence of coverage may reflect current consensus on choice of exchange rate regimes (e.g., flexible exchange rates for the major currency areas).

102. Given the difficulties of ensuring adequate coverage of the "new" issues in Fund surveillance, the observation that in many countries these issues have not been fully integrated into a coherent overall assessment is perhaps not surprising. Without a thorough understanding of the individual elements, their integration into an overall assessment is inevitably superficial. Indeed, in some countries where the quality of coverage was high in all areas, lack of integration has typically not been a problem. This suggests that the quality of Fund surveillance under the broadened framework will primarily depend on the quality of coverage of its elements. Strengthening the coverage of "new" elements will thus likely be critical for the overall effectiveness of surveillance.

IV. Article IV Consultation Procedures

A. Introduction

103. As noted in Chapter II, the Fund relies on various modes, both formal and informal, to ensure comprehensiveness and continuity in its surveillance activities. Nevertheless, Article IV consultations have remained the cornerstone of the Fund's bilateral surveillance. Given the central role of these consultations in the surveillance process, consultation procedures have repeatedly been subjected to intense scrutiny, typically motivated by concerns about continuity of surveillance or strained staff resources. In 1997, the Executive Board sought to address the latter by "encourag[ing] flexibility regarding consultation frequency, mission size, and documentation, particularly in cases where economic developments appeared to be on a positive track." More recently, in June 2001, and again in January 2002, the Board returned to the issue of flexibility in consultation procedures in the context of the discussions on proposals for reducing work pressures. Of the four proposals concerning consultation procedures discussed at the time, the proposal to eliminate reports on Recent Economic Developments (REDs) was adopted in January 2002, while three remaining proposals—the lengthening of consultation cycles in program countries, the use of streamlined consultations, and the modification of requirements for the preparation of Statistical Appendices—were postponed for consideration in the context of this biennial surveillance review. This chapter discusses the latter proposals against the background of a brief review of developments in consultation procedures in 2000-01. The proposal to lengthen the consultation cycle for program countries is addressed in the companion paper on surveillance in a program environment.

B. Consultation Procedures in 2000–2001

Cycles, Frequency, and Delays

104. At end-1999, following efforts undertaken in 1997-98 to make greater use of longer consultation cycles, 160 out of 182 members were on a 12-month consultation cycle, one member was on an 18-month consultation cycle, and 21 were on a 24-month consultation cycle. During 2000-2001, four member countries—Iceland, Libya, the Seychelles and St. Kitts and Nevis—were shifted from a 24-month to a 12-month cycle. In three cases—Iceland, the Seychelles, St. Kitts and Nevis—the shift to an annual cycle was prompted by concerns about large external or domestic imbalances and an ensuing desire to follow economic developments more closely. For Libya, the shift reflected a shared desire for closer collaboration in a situation where the authorities were likely to face important macroeconomic choices for the foreseeable future. As a result, at end-2001, 164 countries were on a 12-month consultation cycle and 18 on a longer cycle.[34]

105. Notwithstanding these changes in consultation cycles, the number of Article IV consultations concluded by the Board declined from an average of 132 per year during 1998-99 to an average of 125 in 2000-01.[35] Coverage of Article IV consultations—i.e., the share of members with which consultations were concluded in a given year—fell from an average of 72 percent of the membership in 1998-99 to 67 percent in 2000-01 (Table 2).[36]

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[34] As of end 2001, the 18 member countries on longer cycles were: Bahrain (18-month cycle); Bahamas, Bahrain, Bhutan, Cyprus, Denmark, Fiji, Kiribati, Luxembourg, Malta, Marshall Islands, Micronesia, Palau, Qatar, Samoa, San Marino, Solomon Islands, St. Lucia, and Vanuatu (all on 24-month cycle). Aruba and the Netherlands Antilles, with which consultation discussions are held in the context of the Article IV consultations with the Netherlands, are also on the 24-month cycle. The consultation cycle for the FR Yugoslavia, which succeeded to the membership of the SFR Yugoslavia in December 2000, will be set at the time of the conclusion of the forthcoming Article IV consultation.

[35] Including consultation discussions with three non-members held during 2000-01: Aruba, Netherlands Antilles, and Hong Kong, S.A.R..

[36] Based only on consultations with Fund members.

Table 2. Indicators Related to Article IV Consultations, 1992-2001

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Coverage and frequency										
Consultations concluded by Board 1/	88	127	138	145	142	130	126	138	123	126
Membership coverage (in percent)	50	70	75	79	78	70	69	74	67	68
Average interval since last consultation (months)	16.7	17.2	16.3	15.7	15.1	15	15.3	16.7	17.9	17.6
Missions										
Number of consultation missions	132	164	168	184	179	166	160	167	165	170
Average size of missions 2/	4.4	4.8	5.2	5.1	5.0	4.9	4.6	4.8	4.4	4.2
Reporting										
Number of staff reports issued	109	130	143	141	140	134	132	136	118	128
Average length of staff reports (pages) 3/	14.9	15.7	16.2	16.1	16.7	18.7	19.6	20.0	19.8	20.6
Number of REDS issued 4/	53	90	93	69	76	96	86	89	84	77
Average length of REDs (pages)	81	91	90	95	92	108	102	101	101	87
Executive Board discussion										
Total Board hours on consultations 5/	160	217	208	232	208	277	203	223	223	217
In percentage of total Board hours	38	46	38	40	41	45	36	35	29	32
Average Board hours per consultation	1.8	1.7	1.5	1.6	1.5	2.1	1.6	1.6	1.8	1.7
Memorandum items:										
Number of program countries 6/	49	44	55	61	61	57	60	58	67	72
Number of country items discussed by Board 7/	253	232	209	225	190	195	191	186	196	191

Sources: Office of Budget and Planning, and the Policy Development and Review and Secretary's Departments.

1/ Including consultations which were concluded on a lapse-of-time basis.
2/ Excluding assistants.
3/ Main text up to and including staff appraisal and excluding decisions, tables and graphs.
4/ For 1994-1996, includes text and tables, and excludes charts. For 1997-1999, includes text, tables, and charts. The change is due to the
5/ Including consultations combined with use of Fund resources and with overdue obligations reports.
6/ For 1992-1999, as of December of each year and for 2000-01, as of the date of consulstation discussion by the Board, excluding compensatory
7/ Including consultations, use of Fund resources, and reports on overdue obligations.

The decline in coverage occurred in all country groups, but it was particularly pronounced for non-G-10 industrial countries, emerging market and developing countries under a Fund program, and transition countries (Table 3).

106. The frequency of Article IV consultations continued to decline as evidenced by a lengthening of the average interval between consultations from 16 months in 1998-99 to 18 months in 2000-01 (Table 4). In 2000-01, as in the past, the consultations with G-10 members have effectively taken place on an annual cycle; for most other groups, the effective cycles have been on average in the 14-16 month range; for developing countries, they were around 18 months on average (Figure 5). In general, consultation frequency was lower for program countries than for non-program countries, except for the developing country group where countries on a longer consultation cycle are concentrated.

107. Underlying the effective lengthening of consultation cycles in recent years has been an increase in delays of consultations. Delays beyond the three-month grace period for countries on the 12-month consultation cycle, which had surged in 1999, remained high during 2000-01 (Table 5). In most of these cases, the delay was relatively short, typically less than two months. As in previous years (with the exception of 1999), the two most frequent reasons for delays were a desire to combine the Article IV consultation with a request for, or a review of, a Fund-supported program and unsettled political conditions or changes in the composition of governments.

108. Requests for extension of the 3-month period between the end of Article IV Consultation discussions between staff and the authorities and the conclusion of the consultation by the Executive Board have also risen. The primary reason for such requests has been Board scheduling conflicts, which were particularly acute around the time of the Spring and Annual Meetings. However, the increase in the average time elapsed between the two above-mentioned dates has been relatively small; and most consultations were completed within the time limit (Tables 6 and 7).[37]

[37] Delays in the conclusion of Article IV consultation beyond the stipulated three-month period require Board approval. In practice, this procedure is administered flexibly: if a Board discussion is scheduled only a few Board days after the deadline, Board approval is not normally sought. Since July 1991, requests for extension have been included in the monthly *Reports on Delayed Completion of Article IV Consultation and Extension of Exchange Measures* and are proposed for approval on a lapse-of-time basis.

Table 3. Article IV Consultations—Membership Coverage, 1996-2001

	1996	1997	1998	1999	2000	2001
	(Number of consultations)					
Consultations concluded by Executive Board 1/ 2/	**142**	**130**	**126**	**138**	**123**	**126**
Industrial countries	23	22	19	22	21	19
G-10	11	11	10	11	11	11
Non-G-10	12	11	9	11	10	8
Emerging markets	14	11	16	16	28	28
Program countries	4	3	6	8	13	10
Non-program	10	8	10	8	15	18
Developing countries	83	75	67	78	59	70
Program countries	30	28	23	27	28	27
Non-program	53	47	44	51	31	43
Countries in transition	22	22	24	22	15	9
Program countries 3/	14	12	12	11	8	7
Non-program	8	10	12	11	7	2
	(In percent of membership)					
Coverage 4/	**78**	**70**	**69**	**74**	**67**	**68**
Industrial countries	96	92	79	92	84	76
G-10	100	100	91	100	100	100
Non-G-10	92	85	69	85	71	57
Emerging markets	81	63	94	94	78	75
Program countries	80	50	86	80	65	56
Non-program	82	70	100	100	88	94
Developing countries	73	65	60	68	57	66
Program countries	79	80	64	87	72	66
Non-program	70	58	58	60	48	66
Countries in transition	73	73	80	73	79	47
Program countries 3/	78	75	71	65	100	54
Non-program	67	71	92	85	64	33
Memorandum items (in absolute numbers):						
Staff reports issued	140	134	132	136	118	128
Consultation missions 5/	179	166	160	167	165	170
Total membership	**181**	**182**	**182**	**182**	**183**	**183**
Industrial countries	24	24	24	24	25	25
G-10	11	11	11	11	11	11
Other	13	13	13	13	14	14
Emerging markets	16	16	16	16	36	36
Program countries	5	6	7	10	20	18
Non-program	11	10	9	6	16	18
Developing countries	111	112	112	112	103	103
Program countries	38	35	36	31	39	41
Non-program	73	77	76	81	64	62
Countries in transition	30	30	30	30	19	19
Program countries 3/	18	16	17	17	8	13
Non-program	12	14	13	13	11	6

Source: Policy Development and Review Department.

1/ Includes consultations with Finland and Sweden in 2000 and Austria, Kuwait, Malta, and Singapre in 2001, which were concluded on a lapse–of–time basis without Executive Board discussion.

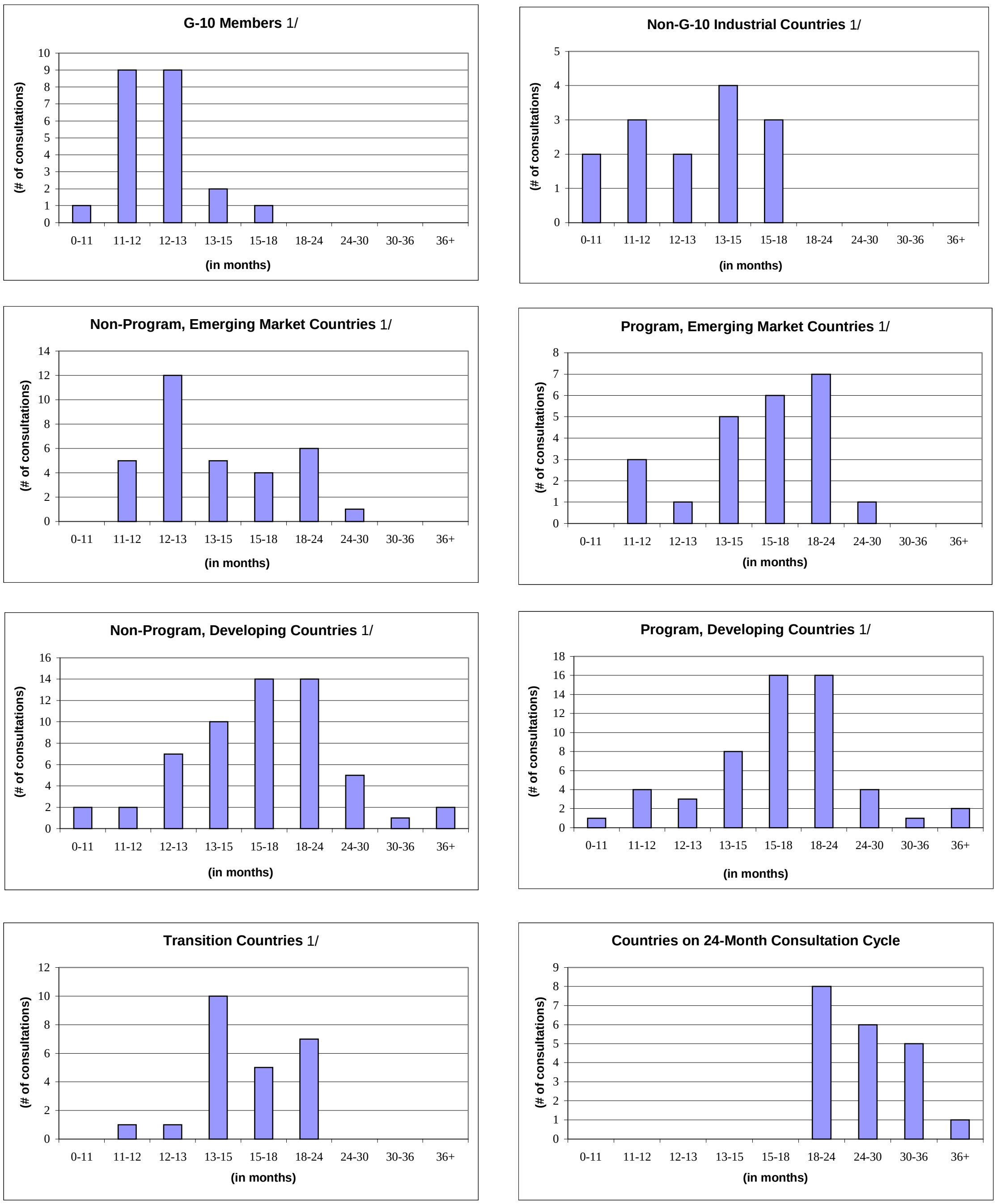
2/ Includes consultation discussions with Aruba and the Netherlands Antilles at the request of the Netherlands' authorities, with Hong Kong at the request of UK authorities, with Hong Kong SAR at the request of the People's Republic of China's authorities, and with Macau at the request of Portugal's authorities.

3/ Excludes arrangements under the systemic transformation facility.

4/ Members only, excluding consultation discussions with Aruba, Hong Kong, Hong Kong SAR, the Netherlands Antilles, and Macau.

5/ Includes multiple missions for individual consultations.

Figure 5. Intervals between Article IV Consultations in 2000-01



Source: Policy Development and Review Department.

1/ Covering only countries on the 12-month consultation cycle.

Table 4. Frequency of Article IV Consultations, 1996-2001

Average interval since last consultation
(In months)

	1996	1997	1998	1999	2000	2001
Consultations concluded by the Executive Board 1/						
All countries	15.1	15.0	15.3	16.7	17.9	17.6
Of which: countries on 12-month cycle	14.7	14.7	14.7	15.8	17.4	16.6
Industrial countries	13.6	12.3	13.5	15.4	13.4	14.6
Of which: G-10	13.0	11.8	12.2	13.0	11.7	12.9
Non G-10	14.2	12.8	14.9	17.8	15.4	16.9
Emerging markets	13.3	13.6	14.1	14.4	15.9	14.9
Of which: program	14.4	13.7	13.9	15.9	17.0	15.7
Non program	12.3	13.6	14.2	12.8	15.0	14.5
Developing countries	15.9	15.7	16.4	17.9	20.9	19.8
Of which: program	15.6	15.0	15.8	16.2	19.3	18.8
Non program	16.1	16.2	16.6	18.8	22.4	20.4
Countries in transition	14.9	16.2	14.5	15.8	16.4	15.5
Of which: program 2/	14.4	16.7	15.9	16.3	16.3	16.1
Non program	15.9	15.5	13.2	15.2	16.6	13.3
Countries without consultations 3/						
Number of countries	40	55	57	48	60	60
Of which: program	13	14	19	12	18	28
Countries without a consultation for more than 24 months	5	4	10	11	11	11

Source: Policy Development and Review Department.

1/ Includes consultation discussions with Aruba and the Netherlands Antilles at the request of the Netherlands' authorities, with Hong Kong at the request of UK authorities, with Hong Kong SAR at the request of the People's Republic of China's authorities, and with Macau at the request of Portugal's authorities.

2/ Excludes arrangements under the systemic transformation facility.

3/ Member countries not concluding consultations with the Executive Board.

Table 5. Reasons for Delays and Further Delays in Completion of Article IV Consultations, 1996-2001

(Number of cases)

	1996	1997	1998	1999	2000	2001
Change of government, change within government, or unstable political situation	17	18	15	20	25	25
Scheduling conflicts	6	5	3	20	17	13
Issuance of staff report delayed pending additional data or action by the authorities 1/	3	4	7	6	8	8
Desire to combine consultation with program request or review	35	30	32	35	56	50
Request of the authorities	4	5	11	15	6	9
Staff constraints	9	11	14	29	12	10
Ongoing policy discussions	0	0	4	9	3	2
Total	**74**	**73**	**86**	**134**	**127**	**117**
By region						
Africa	21	23	34	33	56	46
Asia	8	9	11	16	18	19
Europe	18	15	14	32	19	24
Middle East	7	7	5	12	12	6
Western Hemisphere	20	19	22	41	22	22
Total	74	73	86	134	127	117
Memorandum items:						
Number of countries involved in delays in completion of Article IV consultations 2/	57	56	54	87	76	69

Source: Policy Development and Review Department

1/ Including the staff's decision to incorporate inputs from the FSAP exercise in the Article IV staff report for one case in 2001.

2/ In some cases more than one delay notice was issued for a country–for example, on occasion the revised date for a delayed consultation proved unattainable, necessitating a further delay. Thus, the number of delays and further delays will exceed the number of countries in delay.

Table 6. Article IV Consultations—Time Lapsed Between Termination of Discussions with the Staff and Board Consideration, 1996-2001 1/

(Average number of days)

	1996	1997	1998	1999	2000	2001
Industrial countries	83.2	83.8	87.6	90.8	82.6	83.9
G–7	71.9	74.8	77.0	85.2	81.7	73.9
Non G–7	88.2	88.0	92.5	93.3	83.0	89.8
G–10	76.2	77.8	82.5	90.4	82.2	78.3
Non G–10	89.2	89.8	93.3	91.0	83.0	91.8
Emerging markets 2/	78.4	77.6	81.7	52.0	75.2	77.2
Program	62.3	63.0	63.3	41.0	61.2	73.8
Non program	84.8	83.1	86.7	66.7	87.3	79.1
Developing countries	85.2	89.6	78.5	83.3	86.7	86.9
Program	78.7	79.5	70.0	69.2	78.8	75.1
Non program	89.2	95.6	83.8	90.1	93.9	94.3
Countries in transition 2/	67.7	69.5	79.2	60.3	88.1	80.6
Program	60.2	64.3	70.5	50.0	75.5	79.9
Non program	79.2	75.6	88.7	73.4	102.4	83.0
All countries	81.6	84.2	80.4	77.8	83.6	83.8
			(Percentage distribution)			
50 days or less	14	11	13	22	11	10
51–65 days	9	10	12	13	14	17
66–80 days	19	21	23	21	19	23
81–95 days	32	28	26	22	31	20
More than 95 days	26	29	26	22	26	31

Source: Policy Development and Review Department

1/ Recorded as the year in which the consultation discussions with the staff are terminated.
2/ Excludes arrangements under the systemic transformation facility.

Table 7. Reasons for Request for Extension of the Three-Month Period for the Conclusion of Article IV Consultations, 1996-2001

(Number of cases) 1/

	1996	1997	1998	1999	2000	2001
Scheduling conflicts 2/	3	2	5	9	7	15
Desire to discuss jointly use of Fund resources and Article IV consultations	3	1	0	0	2	3
Additional information or discussion required, e.g., policy or institutional changes	1	0	0	0	5	4
Staff committed to other missions or other duties	0	0	1	2	6	2
Delays at the request of the authorities	2	1	0	1	1	1
Total	**9**	**4**	**6**	**12**	**21**	**25**

Source: Policy Development and Review Department

1/ Individual countries may have had more than one request for extension in a given year.

2/ Most on account of heavy Executive Board schedules, often around the time of the IMFC Spring meeting and Annual Meetings, but also including cases where the Executive Director elected by the member concerned was unable to be present.

Documentation, Board Discussions, and Publication

109. Documentation of Article IV consultations remained extensive. The length of staff reports, which are produced for all consultations, has risen steadily since 1994, reflecting in part the broadening of the range of issues covered in Article IV consultations (Table 8). Including text, tables, boxes, graphs, and appendices, Article IV consultation reports lengthened from an average of 52 pages in 1998-99 to 56 pages in 2000-01. A substantial share of this increase was accounted for by longer annexes and appendixes; for the great majority of staff reports, the main text comprised between 15 and 24 pages.

Table 8. Average Length of Article IV Consultation Staff Reports, 1996-2001 1/

(In number of pages)

	1996	1997	1998	1999	2000	2001
Article IV staff reports						
Average length of main text 2/	16.7	18.7	19.6	20.0	19.8	20.6
Percentage distribution						
14 pages or less	34.5	15.7	9.1	10.3	12.7	7.8
15-19 pages	43.9	43.3	46.2	41.9	32.2	36.7
20-24 pages	19.4	30.6	31.8	33.1	39.0	38.3
25-29 pages	2.2	9.0	9.8	10.3	11.9	12.5
30 pages or more	0.0	1.5	3.0	4.4	4.2	4.7
Article IV only staff reports						
Average length of main text 2/	15.8	18.1	18.8	19.2	18.2	19.9
Percentage distribution						
14 pages or less	34.5	17.5	12.8	13.4	16.2	10.7
15-19 pages	42.4	46.4	47.9	45.4	36.5	41.7
20-24 pages	12	28.9	29.8	30.9	32.4	33.3
25-29 pages	2.2	7.2	6.4	6.2	12.2	8.3
30 pages or more	0.0	0.0	3.2	4.1	2.7	6.0
Article IV and UFR reports						
Average length of main text 2/	18.4	20.3	21.4	21.8	22.6	21.9
Percentage distribution						
14 pages or less	14.9	10.8	0.0	2.6	6.8	2.3
15-19 pages	46.8	35.1	42.1	33.3	25.0	27.3
20-24 pages	34.0	35.1	36.8	38.5	50.0	47.7
25-29 pages	4.3	13.5	18.4	20.5	11.4	20.5
30 pages or more	0.0	5.4	2.6	5.1	6.8	2.3
Reports on Recent Economic Developments 3/						
Average length (pages)	91.7	107.5	102.3	101.1	100.8	86.8
Percentage distribution						
50 pages or less	8.1	0.0	4.7	6.7	8.6	3.7
51-60 pages	2.7	2.1	2.3	3.4	5.7	14.8
61-70 pages	9.5	9.4	9.3	11.2	14.3	18.5
71-80 pages	16.2	13.5	9.3	10.1	8.6	22.2
81-90 pages	17.6	8.3	17.4	16.9	8.6	0.0
91-100 pages	17.6	10.4	11.6	10.1	11.4	14.8
101 pages or more	28.4	56.3	45.3	41.6	42.9	25.9
Memorandum items:						
Staff Report average total length 4/	42.1	46.9	51.4	53.3	55.9	56.5
Average length of main text of staff reports of the largest 25 members (in terms of quota) 2/ 5/	18.7	21.5	22.4	22.3	19.0	24.6
Average length of main text of staff reports of other members 2/ 5/	16.1	17.1	17.7	18.5	20.0	19.6

Source: Policy Development and Review Department.

1/ Data refer to the year in which the staff report was issued.
2/ Main text up to and including staff appraisal.
3/ For 1994-1996, includes text and tables, and excludes charts. For 1997-1999, includes text, tables, and charts. The change is to the revision in document formats which included page numbers for charts. Category includes REDs and background papgers, excludes statistical appendices.
4/ Text, tables, graphs and appendices.
5/ The figures are for stand-alone staff reports.

110. Background documentation for Article IV consultations took the form of Recent Economic Developments (RED) reports, Statistical Appendices (SA), reports on Selected Issues (SI), and combined SI/RED or SI/SA reports.[38] Production of REDs continued to fall in 2000-01 while, proportionally, production of SI/RED, SI/SA and SA rose. Background documentation was limited to an SI paper (without a section on recent economic developments or a statistical appendix) in about 20 percent of consultations. This practice was generally followed for—and only for—advanced economies. In rare cases (6 in 2000 and 4 in 2001), there was no background documentation. After rising steadily in the 1990s, the average length of background documents declined substantially in 2001 for both REDs and SIs; the average length of SAs remained around 50 pages.

111. In addition to these documents, the FSAP and the work on standards and codes have resulted since 1999 in the preparation of FSSA reports and ROSC modules, which also provide background information for Board discussions of Article IV consultations. FSSA reports were prepared for 7 consultations concluded in 2000 and 18 consultations in 2001. 45 ROSCs—in 2000—and 112 ROSCs—in 2001—were issued to the Board, including ROSCs incorporated in FSSA reports.

112. Of the 249 Article IV consultations concluded by the Executive Board in 2000 and 2001, all but six were concluded with a Board discussion. The remaining six consultations were completed on a lapse-of-time basis (Finland (2000), Sweden (2000), Austria (2001), Kuwait (2001), Malta (2001), Singapore (2001)).

113. Press Information Notices (PINs) were published for 102 Article IV consultations in 2000 and 107 consultations in 2001. Thus, in 2000-01, PINs were published for 84 percent of all consultations. Staff reports were published for 57 consultations concluded in 2000 and 72 consultations concluded in 2001. These figures represented 46 and 57 percent of all consultations concluded in these respective years.

Use of Staff and Board Resources

114. Recent developments in staff resources devoted to surveillance suggest a shift from activities directly related to Article IV consultations to other surveillance activities, including work on FSAPs and ROSCs. Staff resources devoted to Article IV consultations, including consultations combined with discussions on use of Fund resources, declined from an average of 186 staff years in FY1998-99 to 180 staff years in FY2000-01 (Table 9). The average size of surveillance missions has continued to decline from 4.7 persons (excluding assistants) in FY1998-99 to 4.3 persons in FY2000-01. By contrast, staff resources devoted to other

[38] Combined RED/SI reports consist of one or more chapters on recent economic developments, one or more chapters on selected issues, and a statistical appendix.

Table 9. Staff Resources Devoted to Country-Specific Surveillance and Program Activities, FY 1996-2001 1/

	FY 1996	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001
	(In staff years)					
Article IV consultations only	120.7	131.8	117.3	119.3	117.8	110.3
Article IV consultations combined with use of Fund resources	60.9	53.3	68.8	67.2	71.2	61.3
Associated country-specific activities 2/	188.3	186.7	165.8	161.1	150.6	191.9
Total resources devoted to bilateral surveillance	369.9	371.8	351.9	347.6	339.6	363.5
Program only	218.8	211.1	199.4	256.5	243.6	258.2
Associated country-specific activities 2/	80.7	80.0	88.5	41.5	82.7	93.6
Total resources devoted to program only activities	299.5	291.1	287.9	298.1	326.4	351.8
Total staff resources devoted to country-specific surveillance and program activities	669.4	662.9	639.9	645.7	665.9	715.4
Of which: mission travel	91.4	90.6	89.4	96.2	102.6	114.5
	(As a percent of total country-specific work)					
Article IV consultations only	18.0	19.9	18.3	18.5	17.7	15.4
Article IV consultations combined with use of Fund resources	9.1	8.0	10.8	10.4	10.7	8.6
Associated country-specific activities 2/	28.1	28.2	25.9	24.9	22.6	26.8
Total resources devoted to bilateral surveillance	55.3	56.1	55.0	53.8	51.0	50.8
Program only	32.7	31.8	31.2	39.7	36.6	36.1
Associated country-specific activities 2/	12.1	12.1	13.8	6.4	12.4	13.1
Total resources devoted to program only activities	44.7	43.9	45.0	46.2	49.0	49.2
Total staff resources devoted to country-specific surveillance and program activities	100.0	100.0	100.0	100.0	100.0	100.0
Of which: mission travel	13.7	13.7	14.0	14.9	15.4	16.0
Memorandum item (in staff years):						
Noncountry-specific surveillance and program activities	273.6	290.5	355.5	367.8	395.9	414.0
Of which: surveillance (non program) activities	...	...	266.8	284.6	303.6	318.4
program activities	...	...	88.7	83.2	92.3	95.7

Source: Office of Budget and Planning.

1/ Excludes technical assistance.

2/ For FY96 and FY97, sub-categories were interpolated on the basis of data for FY98 and FY99.

country-specific surveillance activities—including monitoring between Article IV consultations, work on FSAPs and ROSCS—rose from an annual average of 163 staff years in FY 1998-99 to 171 staff years in FY 2000-01. [39]

115. Growth of non-country-specific surveillance and program activities continued unabated in FY 2000-01, absorbing an annual average of 311 staff years compared with 276 staff years per year in FY1998-99. This development primarily reflected increased use of resources on policy development, research, and evaluation activities, which may be traced to the flurry of policy initiatives undertaken in recent years, including initiatives to strengthen the architecture of the international monetary system.

116. While the time spent by the Executive Board on Article IV consultations has increased from an annual average of 213 hours in FY 1998-99 to 220 hours in FY 2000-01, the share of these discussions in total Board time has continued to decline. On average, the Board devoted 1.7 hours per consultation in FY2000-01, slightly more than in FY1998-99.

C. Flexibility in Article IV Consultation Procedures

117. While the staff resources devoted to Article IV surveillance activities have declined in recent years, both in absolute terms and as a share of total resources used for surveillance, Article IV consultations continue to account for about one quarter of the Fund surveillance activities and one half of bilateral surveillance. Thus, it is worth considering how these consultations can be conducted most efficiently without jeopardizing the effectiveness of Fund surveillance.

118. As noted in the introduction, two proposals that emerged from the initiative to reduce work pressures are under consideration: (i) to introduce a streamlined consultation procedure, which would produce a short staff report focusing on a few key issues, and involve no background documentation, and could be concluded by the Board on a lapse-of-time basis;[40] (ii) to modify requirements for the preparation of Statistical Appendices. These proposals relate to three elements of Article IV consultation procedures which are addressed below: (i) the scope of the discussions and staff report; (ii) the requirements applying to background documentation; and (iii) the nature of the Board conclusion of the Article IV consultation. In addition, it seems useful to discuss the lessons from the experience with the policy of greater flexibility in consultation cycles.

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[39] Budget Reporting System (BRS) data indicate that 39 staff years were devoted to the FSAP and ROSCs in FY 2001. This figure is likely to be biased downward.

[40] The proposed procedures also included an expectation that a streamlined consultation would be followed by a full consultation; and stated that a streamlined consultation could only be used for members for which no pressing issues were apparent.

Consultation Cycles

119. The move toward greater flexibility in consultation cycles, which was encouraged by the Executive Board at the conclusion of the 1997 biennial surveillance review, appears to have met with limited success. Between mid-1997 and early 1999, only 15 countries were shifted to a 24-month cycle, raising the total number of countries on a longer consultation cycle to 22, or 12 percent of the membership.[41] This limited success may largely be explained by the reluctance of many member countries to accept a longer consultation cycle and thus, in their view, to appear to be treated differently than the majority of the membership. In addition, greater use of the flexibility afforded by the current policy on consultation cycles appears to have been constrained by concerns about developments in member countries and a perceived need for close surveillance. As indicated above, since 1999, three countries have been shifted from a 24-month cycle to a 12-month cycle in light of such concerns.

120. While the move towards longer *de jure* consultation cycles has been limited, effective consultation cycles for many member countries have been considerably longer than the specified cycles in the past two years, particularly for developing countries. The average interval between two consultations in 2000-01 was 19.2 months for developing countries on a 12-month consultation cycle; the median interval was 16.7 months—nearly five months longer than the *de jure* cycle of these countries.[42]

121. This experience suggests that while it is desirable to maintain the flexibility on consultation cycles afforded by the current policy, efforts to encourage broader application in the case of non-program countries would likely yield little benefit.

The Scope of Staff Reports

122. At the conclusion of the 1997 biennial surveillance review, Executive Directors encouraged staff to increase efforts to inject greater flexibility and discretion in deciding the nature and scope of Article IV consultation documentation, including the scope of staff reports. These calls for flexibility in consultation documentation were reiterated at the conclusion of the 2000 biennial review of surveillance and are reflected in the proposed streamlined consultation procedure. The current policy on consultation procedures thus

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[41] At end-1996, 6 countries (Libya, Luxembourg, Malta, St. Lucia, St Kitts-Nevis, and San Marino) were on a 24-month consultation cycle and one (Bahrain) was on an 18-month consultation cycle. Between mid-1997 and early 1999, the following 15 countries were shifted from a 12-month to a 24-month consultation cycle: Bahamas, Bhutan, Cyprus, Denmark, Fiji, Iceland, Kiribati, Marshall Islands, Micronesia, Palau, Qatar, Samoa, Seychelles, Solomon Islands, and Vanuatu.

[42] The median intervals between consultations in 2000-01 for all countries on a 12-month consultation cycle and for developing countries on a 12-month consultation cycle were respectively 15.1 and 16.7 months. The median intervals are lower than the average intervals, due to the presence of fat tails in the distribution of intervals between consultations across members.

accommodates, in principle, the option of producing staff reports focusing on a few key issues, which is one of the elements of the proposed streamlined consultation procedure.

123. Evidently, in applying the flexibility afforded by current procedures, care needs to be taken that all important issues concerning a country's macroeconomic stability and external viability receive adequate coverage. In countries where no major issues are apparent—the cases that would be eligible for the streamlined procedure—the required coverage may indeed be relatively limited. However, in order to establish that no major issues are apparent, staff needs to be informed on a broad range of potentially relevant issues. Focused discussions and staff reports are not tantamount to limited surveillance.

Background Documentation

124. At the 1997 biennial surveillance review, Directors also encouraged staff to use greater flexibility and discretion in deciding on the nature and scope of background documentation for Article IV consultations. They felt, however, that RED reports remain useful in many cases, particularly for many of the smaller developing countries where these reports often represent the only major source of comprehensive economic information and analysis. They agreed that in those cases, "there would continue to be an expectation that an RED report would be prepared every other year." This guidance introduced the option of not producing background documentation for Article IV consultations in some instances. Thus, the second element of the proposed streamlined consultation procedure—no background documentation—has also been part of the policy on consultation procedures since 1997. However, this option was rarely used—in 6 instances in 2000 and in 4 cases in 2001—and it seems worth encouraging flexibility further.

125. The two proposals concerning background documentation for Article IV consultations that were put forward in the context of proposals for reducing work pressures provide for additional flexibility. The decision to abolish RED reports requires staff to include, as needed, appropriate information on recent economic developments every other year in a Selected Issues paper. This requirement focuses on countries where such information is not readily available and allows room for judgment on the need for such information.

126. Similarly, it is proposed to leave the judgment on the need for a Statistical Appendix for a given Article IV consultation to the area department, in close consultation with the Executive Director for the member concerned. In arriving at this judgment, staff would be guided by Executive Directors' need for adequate information for effective surveillance and the extent to which statistical information for the country concerned is readily available to the public.

127. In deciding on the need for information on recent economic developments, on a Statistical Appendix, and on other background information for an Article IV consultation, staff would need to ensure that adequate background documentation is available to support the analysis in the staff report. In some instances, there may be no need for any background

documentation—as envisaged under the proposed streamlined procedure. In these cases, as in all other cases, staff would be accountable for its decision at the time of the Board discussion.

Board Conclusion

128. The third, optional, element of the proposed streamlined consultation procedure is the conclusion of the consultation by the Executive Board on a lapse of time (LOT) basis. The Executive Board discussed the use of LOT procedures for completion of Article IV consultations in October 1996, following two *ad hoc* cases of LOT completion of Article IV consultations. At the time, Directors considered that, while LOT conclusions of Article IV consultations might be appropriate in view of the Board's heavy workload, they should be used only rarely as the Executive Board assessment constituted a critical element of the consultation process and, in principle, all Article IV consultations should be discussed by the Board. In addition to these general principles, the Executive Board set criteria for use of the LOT procedure, including the criterion that it could not be used for two consecutive Article IV consultations, and specified that the decision concluding an Article IV consultation on a LOT basis would state that "*the Executive Board endorses the thrust of the staff appraisal …*"

129. LOT conclusions of Article IV consultations have remained relatively rare. LOT procedures were not used at all during 1996-99, and in the last two years, only six Article IV consultations were completed on a lapse-of-time basis (Finland (2000), Sweden (2000), Austria (2001), Kuwait (2001), Malta (2001), Singapore (2001)). A possible reason for this hesitancy to use the LOT procedure may be that the conclusion of such an Article IV consultation could be seen as not carrying the full endorsement of the Board, notwithstanding the Board's decision stating its endorsement of the thrust of the staff appraisal. In an environment of increased transparency, an added concern may be that the public could view consultations concluded with a Board discussion and consultations concluded on a LOT basis differently.

130. In light of these considerations, it is not clear whether efforts to encourage greater reliance on the LOT procedure in the context of streamlined consultations would elicit a strong response. However, retaining the existing policy, which provides for the occasional use of LOT conclusions, has merit, as it offers a resource-saving method of completing an Article IV consultation.

D. Conclusions

131. The preceding discussion of various elements of Article IV consultation procedures suggests that there is considerable merit in retaining the flexibility afforded by the current policy on consultation cycles for non-program countries, the scope of staff reports, and the LOT conclusion of Article IV consultations. Furthermore, the proposal to leave the judgment on the production of Statistical Appendices to the staff (in consultation with the Executive Director for the country concerned) would provide additional flexibility in producing background documentation for Article IV consultations. It would seem a useful complement

to the recent decision to abolish REDs. Such flexibility could help ease pressures on staff resources without undermining the effectiveness of surveillance. The enhanced flexibility of existing procedures would accommodate all elements of the proposed streamlined consultations, obviating the need for a special consultation procedure.

The 1977 Surveillance Decision (As Amended)

1. The Executive Board has discussed the implementation of Article IV of the proposed Second Amendment of the Articles of Agreement and has approved the attached document entitled “Surveillance Over Exchange Rate Policies”. The Fund shall act in accordance with this document when the Second Amendment becomes effective. In the period before that date the Fund shall continue to conduct consultations in accordance with present procedures and decisions.

2. The Executive Board shall review the document entitled “Surveillance Over Exchange Rate Policies” at intervals of two years and at such other times as consideration of it is placed on the agenda of the Executive Board.

Decision No. 5392-(77/63)
April 29, 1977, as amended by
Decision No. 8564-(87/59), April 1, 1987,
Decision No. 8856-(88/64), April 22, 1988,
and Decision No. 10950-(95/37), April 10, 1995

Surveillance over Exchange Rate Policies

General Principles

Article IV, Section 3(a) provides that “The Fund shall oversee the international monetary system in order to ensure its effective operation, and shall oversee the compliance of each member with its obligations under Section 1 of this Article.” Article IV, Section 3(b) provides that in order to fulfill its functions under 3(a), “The Fund shall exercise firm surveillance over the exchange rate policies of members, and shall adopt specific principles for the guidance of all members with respect to those policies.” Article IV, Section 3(b) also provides that “The principles adopted by the Fund shall be consistent with cooperative arrangements by which members maintain the value of their currencies in relation to the value of the currency or currencies of other members, as well as with other exchange arrangements of a member’s choice consistent with the purpose of the Fund and Section 1 of this Article. These principles shall respect the domestic social and political policies of members, and in applying these principles the Fund shall pay due regard to the circumstances of members.” In addition, Article IV, Section 3(b) requires that “each member shall provide the Fund with the information necessary for such surveillance, and, when requested by the Fund, shall consult with it on the member’s exchange rate policies.”

The principles and procedures set out below, which apply to all members whatever their exchange arrangements and whatever their balance of payments position, are adopted by the Fund in order to perform its functions under Section 3(b). They are not necessarily comprehensive and are subject to reconsideration in the light of experience. They do not deal directly with the Fund's responsibilities referred to in Section 3(a), although it is recognized that there is a close relationship between domestic and international economic policies. This relationship is emphasized in article IV which includes the following provision: "Recognizing…that a principal objective [of the international monetary system] is the continuing development of the orderly underlying conditions that are necessary for financial and economic stability, each member undertakes to collaborate with the Fund and other members to assure orderly exchange arrangements and to promote a stable system of exchange rates."

Principles of Guidance of Members' Exchange Rate Policies

A. A member shall avoid manipulating exchange rates or the international monetary system in order to prevent effective balance of payments adjustment or to gain an unfair competitive advantage over other members.

B. A member should intervene in the exchange market if necessary to counter disorderly conditions which may be characterized inter alia by disruptive short-term movements in the exchange value of its currency.

C. Members should take into account in their intervention policies the interests of other members, including those of the countries in whose currencies they intervene.

Principles of Fund Surveillance over Exchange Rate Policies

1. The surveillance of exchange rate policies shall be adapted to the needs of international adjustment as they develop. The functioning of the international adjustment process shall be kept under review by the Executive Board and Interim Committee and the assessment of its operation shall be taken into account in the implementation of the principles set forth below.

2. In its surveillance of the observance by members of the principles set forth above, the Fund shall consider the following developments as among those which might indicate the need for discussion with a member.

(i) protracted large-scale intervention in one direction in the exchange market;

(ii) an unsustainable level of official or quasi-official borrowing, or excessive and prolonged short-term or quasi-official lending, for balance of payments purposes.

(iii) (a) the introduction, substantial intensification, or prolonged maintenance, for balance of payments purposes, or restrictions on, or incentives for, current transactions or payments, or

(b) the introduction or substantial modification for balance of payments purposes or restrictions on, or incentives for, the inflow or outflow of capital;

(iv) the pursuit, for balance of payments purposes, of monetary and other domestic financial policies that provide abnormal encouragement or discouragement to capital flows; ~~and~~

(v) behavior of exchange rate that appears to be unrelated to underlying economic and financial policies that provide abnormal encouragement or discouragement to capital flows; and

(vi) unsustainable flows of private capital.[43]

3. The Fund's appraisal of a member's exchange rate policies shall be based on an evaluation of the developments in the member's balance of payments, including the size and sustainability of capital flows, against the background of its reserve position and its external indebtedness. This appraisal shall be made within the framework of a comprehensive analysis of the general economic situation and economic policy strategy of the member, and shall recognize that domestic as well as external policies can contribute to timely adjustment of the balance of payments. The appraisal shall take into account the extent to which the policies of the member, including its exchange rate policies, serve the objectives of the continuing development of the orderly underlying conditions that are necessary for financial stability, the promotion of sustained sound economic growth, and reasonable levels of employment.

Procedures for Surveillance

I. Each member shall notify the Fund in appropriate detail within thirty days after Second Amendment becomes effective of the exchange arrangements it intends to apply in fulfillment of its obligations under Article IV, Section I. Each member shall also notify the Fund promptly of any changes in its exchange arrangements.

II. Members shall consult with the Fund regularly under Article IV. In principle, t~~T~~he consultations under Article IV shall comprehend the regular consultations under Articles VIII and XIV, and shall take place annually. ~~In principle, such consultations shall take place annually, and~~ They shall include consideration of the observance by members of the principles set forth above as well as of a member's obligations under Article IV, Section 1. Not later than three months after the termination of discussions between the member and the staff, the Executive Board shall reach conclusions and thereby complete the consultation under Article IV.[44]

[43] This paragraph, as well the following paragraph, were amended on April 10, 1995 by Decision No. 10950-(95/37)

[44] This paragraph was amended on April 1, 1987 by Decision No. 8564-(87/59).

III. Board developments in exchange rates will be reviewed periodically by the Executive Board, inter alia in discussions of the international adjustment process within the framework of the *World Economic Outlook*. The Fund will continue to conduct special consultations in preparing for these discussions.

IV. The Managing Director shall maintain close contact with members in connection with their exchange arrangements and exchange policies, and will be prepared to discuss on the initiative of a member important changes that it contemplates in its exchange arrangements or its exchange rate policies.

V. If, in the interval between Article IV consultations, the Managing Director, taking into account any views that may have been expressed by other members, considers that a member's exchange rate policies may not be in accord with the exchange rate principles, he shall raise the matter informally and confidentially with the member, and shall conclude promptly whether there is a question of observance of the principles. If he concludes that there is such a question, he shall initiate and conduct on a confidential basis a discussion with the member under Article IV, Section 3(b). As soon a possible after the completion of such a discussion, and in any event not later than four months after its initiation, the Managing Director shall report to the Executive Board on the results of the discussion. If, however, the Managing Director is satisfied that the principles are being observed, he shall informally advise all Executive Directors, and the staff shall report on the discussion in the context of the next Article IV consultation; but the Managing Director shall not place the matter on the agenda of the Executive Board unless the member requests that this procedure be followed.

VI. The Executive Board shall review ~~annually~~ the general implementation of the Fund's surveillance over members' exchange rate policies at intervals of two years and at such other times as consideration of it is placed on the agenda of the Executive Board.[45]

[45] This paragraph was amended on April 22, 1988 by Decision No. 8856-(88/64).

Appendix Table 1. Sample of Non-Program Countries, 2000-01

Major Advanced Economies	***Other Advanced Economies***	***Emerging-Market Countries***	***Small Developing Countries***	***Oil-Exporting Countries***	***Other Developing Countries***
Canada	Australia	Algeria	Antigua and Barbuda	Bahrain	Bangladesh
France	Belgium	Chile	Bahamas	Equatorial Guinea	Belarus
Germany	Finland	China, P.R.	Barbados	Iran, Islamic Republic of	Botswana
Italy	Ireland	Czech Republic	Belize	Kazakhstan	Namibia
Japan	Netherlands	Egypt	Fiji	Libya	Nepal
United Kingdom	New Zealand	Hong Kong, SAR 1/	Grenada	Saudi Arabia	Suriname
United States	Spain	Hungary	Kiribati	United Arab Emirates	Swaziland
	Sweden	India	Maldives		Syria
	Switzerland	Israel	Mauritius		Uzbekistan
		Korea	Netherlands, Antilles 1/		
		Lebanon	Palau		
		Malaysia	St. Vincent and the Grenadines		
		Mexico	Vanuatu		
		Morocco			
		Philippines			
		Poland			
		Russia			
		Singapore			
		Slovak Republic			
		Slovenia			
		South Africa			
		Thailand			
		Uruguay			
		Venezuela			

1/ Region or territory of member country for which separate Article IV consultations are conducted.

Appendix Table 2. Classification of Fund Members by Country Groups

Developing Countries

- Afghanistan
- Angola
- Antigua and Barbuda
- Aruba 1/
- Bahamas, The
- Bahrain
- Bangladesh
- Barbados
- Belize
- Benin * ^
- Bhutan
- Bolivia * ^
- Botswana
- Brunei Darussalam
- Burkina Faso * ^
- Burundi
- Cameroon * ^
- Cape Verde *
- Central African Republic * ^
- Chad * ^
- Comoros ^
- Congo, Dem. Rep. of the ^
- Congo, Rep. Of *
- Costa Rica
- Cote d' Ivoire * ^
- Djibouti * ^
- Dominica
- Dominican Rep.
- Ecuador * ^
- El Salvador *
- Equatorial Guinea
- Eritrea
- Ethiopia ^
- Fiji
- Gabon * ^
- Gambia, The * ^
- Ghana * ^
- Grenada
- Guatemala
- Guinea * ^
- Guinea-Bissau * ^
- Guyana * ^
- Haiti
- Honduras * ^
- Iran, Islamic Rep. Of
- Iraq
- Jamaica ^
- Kenya * ^
- Kiribati
- Kuwait
- Lesotho ^
- Liberia
- Libya
- Madagascar * ^
- Malawi * ^
- Maldives
- Mali * ^
- Malta
- Marshall Islands
- Mauritania * ^
- Mauritius
- Micronesia
- Mozambique * ^
- Myanmar
- Namibia
- Nepal
- Netherlands Antilles 1/
- Nicaragua * ^
- Niger * ^
- Nigeria * ^
- Oman
- Pakistan *
- Palau
- Panama * ^
- Papua New Guinea * ^
- Paraguay
- Qatar
- Rwanda * ^
- Samoa
- Sao Tome and Principe * ^
- Saudi Arabia
- Senegal * ^
- Seychelles
- Sierra Leone
- Solomon Islands
- Somalia
- Sri Lanka ^
- St. Kitts and Nevis
- St. Lucia
- St. Vincent
- Sudan *
- Suriname
- Swaziland
- Syrian Arab Rep
- Tanzania * ^
- Togo ^
- Tonga
- Trinidad and Tobago
- Tunisia
- U.A.E.
- Uganda * ^
- Vanuatu
- Yemen * ^
- Zambia * ^
- Zimbabwe

Emerging Market Countries

- Algeria ^
- Argentina
- Brazil * ^
- Bulgaria * ^
- Chile
- China, P.R. of
- Colombia * ^
- Croatia * ^
- Czech Republic
- Egypt
- Estonia * ^
- Hong Kong 1/
- Hungary
- India
- Indonesia * ^
- Israel
- Jordan * ^
- Korea * ^
- Latvia * ^
- Lebanon
- Lithuania * ^
- Malaysia
- Mexico *
- Morocco
- Peru * ^
- Philippines *
- Poland
- Romania * ^
- Russian Federation *
- Singapore
- Slovak Republic
- South Africa
- Thailand * ^
- Turkey * ^
- Ukraine * ^
- Uruguay * ^
- Venezuela

Industrial Countries

- Australia
- Austria
- Belgium
- Canada
- Cyprus
- Denmark
- Finland
- France
- Germany
- Greece
- Iceland
- Ireland
- Italy
- Japan
- Luxembourg
- Netherlands
- New Zealand
- Norway
- Portugal
- San Marino
- Spain
- Sweden
- Switzerland
- United Kingdom
- United States

Transition countries

- Albania * ^
- Armenia ^
- Azerbaijan ^
- Belarus
- Bosnia & Herzegovina * ^
- Cambodia * ^
- Georgia ^
- Kazakhstan * ^
- Kyrgyz Republic * ^
- Lao PDR ^
- Macedonia, FYR ^
- Moldova * ^
- Mongolia *
- Slovenia
- Tajikistan * ^
- Turkmenistan
- Uzbekistan
- Vietnam ^
- Yugoslavia, F.R. of

* = classified as program country in 2000; ^ = classified as program country in 2001; a country was classified as a program country if it had a program in place at the time of its Article IV consultation or, in cases where no Article IV consultation took place in the given year, if it had a program in place by the time the Article IV consultation would have been expected to have been concluded, given the consultation cycle.

1/ Regions that are not Fund members, but for which regular Article IV consultations are conducted.

Appendix Table 3. Exchange Restrictions of Countries with Article VIII Status 1/

Free of Exchange Restrictions/Practices			Maintain Approved Restrictions/Practices	Maintain Unapproved Restrictions/Practices Only
Algeria	Grenada	Norway	Botswana	Belize
Antigua & Barbuda	Guatemala	Oman	Croatia	Guinea 3/
Argentina 2/	Guinea-Bissau	Pakistan	Dominican Republic	India
Armenia	Guyana	Palau	Ecuador 2/	Macedonia, FYR
Australia	Haiti	Panama	Sierra Leone	Seychelles
Austria	Honduras	Papua New Guinea	Russian Federation 4/	Solomon Islands 5/
Bahamas, The	Hungary	Paraguay 2/		St. Lucia
Bahrain	Iceland	Peru 2/	Sub-total	Suriname
Bangladesh	Indonesia	Philippines	**6 countries**	Tunisia
Barbados	Ireland	Poland		Zimbabwe
Belarus	Israel	Portugal		
Belgium	Italy	Qatar		Sub-total
Benin	Jamaica	Romania		**10 countries**
Bolivia 2/	Japan	Rwanda		
Brazil	Jordan	Samoa		**Total, Article VIII Status**
Brunei Darussalam	Kazakhstan	San Marino		**150 countries**
Bulgaria	Kenya	Saudi Arabia		
Burkina Faso	Kiribati	Senegal		
C.A.R.	Korea	Singapore		
Cameroon	Kuwait	Slovak Republic		
Canada	Kyrgyz Republic	Slovenia		
Chad	Latvia	South Africa		
Chile 2/	Lebanon	Spain		
China	Lesotho	Sri Lanka		
Comoros	Lithuania	St. Kitts-Nevis		
Congo, Republic of	Luxembourg	St. Vincent		
Costa Rica	Madagascar	Swaziland		
Cote d' Ivoire	Malawi	Sweden		
Cyprus	Malaysia	Switzerland		
Czech Republic	Mali	Tanzania		
Denmark	Malta	Thailand		
Djibouti	Marshall Islands	Togo		
Dominica	Mauritania 6/	Tonga		
El Salvador	Mauritius	Trinidad & Tobago		
Equatorial Guinea	Mexico 2/	Turkey		
Estonia	Micronesia	U.A.E.		
Fiji	Moldova	Uganda		
Finland	Mongolia	Ukraine		
France	Morocco	United Kingdom		
Gabon	Namibia	United States		
Gambia, The	Nepal	Uruguay 2/		
Georgia	Netherlands	Vanuatu		
Germany	New Zealand	Venezuela 2/		
Ghana	Nicaragua	Yemen		
Greece	Niger			
		Sub-total		
		134 countries		

Source: Policy Development and Review Department.

1/ Except in cases where the country has since accepted the obligations of Article VIII, the table is based on the last Article IV Consultation report. In some instances, restrictions or practices may have been removed or newly introduced since the issue of the last consultation report.

2/ Country's membership in the Latin American Integration Association constitutes an unapproved exchange restriction in the form of a bilateral payments agreement.

3/ In Guinea, owing to the absence of a formal mechanism to ensure that the spread between the official and parallel market rates never exceeds 2 percent, the arrangement constitutes a multiple currency practice.

4/ The Russian Federation has both approved and unapproved exchange restrictions.

5/ In June 2000, Solomon Islands introduced exchange restrictions resulting in delays on the availability of foreign exchange for current international payments.

6/ On April 17, 2000 Mauritania introduced the "Extended Exchange Market" unifying different components of the official exchange market which eliminated the possibility for occurrence of a multiple currency practice.

Appendix Table 4. Exchange Restrictions or Practices of Countries with Article XIV Status 1/

Free of Exchange Restrictions/Practices	Maintain Approved Article VIII Restrictions/Practices	Maintain Unapproved Article VIII Restrictions/Practices	Maintain Unapproved Article XIV Restrictions/Practices Only
Azerbaijan	Ethiopia 2/ 3/	Afghanistan 5/	Bhutan
Bosnia & Herzegovina		Albania 3/	
Cape Verde		Angola 3/	Sub-total
Cambodia	Sub-total	Burundi	**1 country**
Congo, Democratic Rep.	**1 country**	Colombia	
Eritrea 4/		Egypt	**Total, Article XIV Status**
Laos		Iran	**32 countries**
Liberia		Iraq 5/	
Mozambique		Libya 3/	
Sao Tome & Principe		Maldives 6/	
Tajikistan		Myanmar	
		Nigeria	
Sub-total		Somalia 3/	
11 countries		Sudan	
		Syrian Arab Rep. 3/	
		Turkmenistan	
		Uzbekistan	
		Vietnam 3/	
		Zambia 7/	
		Sub-total	
		19 countries	

Source: Policy Development and Review Department.

1/ Except in cases where the country has since accepted the obligations of Article VIII, the table is based on the last Article IV Consultation report. In some instances, restrictions or practices may have been removed since the issue of the last consultation; in other cases, new restrictions subject to Fund jurisdiction under Article VIII may also have been introduced. The Federal Republic of Yugoslavia, currently holding Article XIV status, is not included in this table as there has not been an Article IV consultation since it rejoined the Fund in December 2000.
2/ Country also maintains unapproved Article VIII restrictions.
3/ Country also maintains Article XIV restrictions.
4/ On August 15, 2001 authorities of Eritrea repealed the exchange controls imposed earlier allowing commercial banks and foreign exchange bureaus to freely buy and sell foreign exchange at market-determined exchange rates.
5/ No Article IV consultation has been held with Afghanistan since 1991 and with Iraq since 1980 and the current situation regarding exchange restrictions in these countries is unclear.
6/ In late 2000, Maldives imposed administrative limits on the availability of foreign exchange in the context of a general shortage of hard currency loss.
7/ In Zambia, the continued existence of private external arrears, accumulated prior to October 1985, evidences an exchange restriction under Article VIII, Section 2(a).

Appendix Table 5. Acceptance of Article VIII Status and Nature of Restrictions Maintained, 2000-2001

Country	Date of Acceptance	Free of Restrictions	Type of Restriction	Temporary Approval
Belarus	11/5/01	Y		

Source: Monetary and Exchange Affairs Department.

Appendix Table 6. Exchange Restrictions Approved by the Fund, 2000-2001 1/

Country	*Status*	*Approved Restrictions*	*Approval Status*
Botswana (SM/01/67)	VIII	Multiple currency practice	Approval until March 31, 2002 or the completion of the next Article IV consultation, whichever is earlier.
Croatia (EBS/01/27)	VIII	Freeze on certain foreign currency deposits.	Approval until March 31, 2002 or the completion of the next Article IV consultation, whichever is earlier.
Dominican Republic (SM/01/41)	VIII	Multiple currency practice	Approval until December 31, 2001.
Ecuador (EBS/00/164)	VIII	Freeze on demand and savings deposits with the banking system.	Approval until December 31, 2001.
Ethiopia (EBS/01/13)	XIV	Multiple currency practice	Approval until October 1, 2001 or the conclusion of the next Article IV consultation, whichever is earlier.
Ghana (EBS/00/159)	VIII	Special foreign exchange swap transactions between the Bank of Ghana and commercial banks.	Approval until March 31, 2001 or the conclusion of the next Article IV consultation, whichever is earlier.
Macedonia, FYR (EBS/00/23)	VIII	Freeze on certain foreign currency deposits	Approval until April 30, 2000.
Russian Federation (SM/00/196)	VIII	Limitations imposed upon the convertibility of current proceeds held in nonresident ruble accounts and multiple currency practice.	Approval until September 30, 2001 or the completion of the next Article IV consultation, whichever is earlier.
Sierra Leone (SM/01/9)	VIII	Requirement of a tax clearance certificate for payments and transfers for certain types of current international transactions.	Approval until January 31, 2002.

Source: Policy Development and Review Department.

1/ Restrictions based on national security considerations, which the Fund was notified of in accordance with Decision 144-(52/53), are excluded.