

BUFF/06/66

April 7, 2006

**The Chairman's Summing Up  
Implementing the Fund's Medium-Term Strategy  
Executive Board Meeting 06/33  
April 3, 2006**

**Overview**

Executive Directors have had a very useful discussion on the courses of action put forward in the report on implementing the Fund's medium-term strategy. Although the Executive Board is not yet taking any decisions, we have now a better grasp of the issues that we must address as we move forward from conceptualizing the medium-term strategy to proposing decisions for implementation. In doing so, we will of course need to make sure that we maintain our effort to build a strong consensus.

**Surveillance**

Directors reiterated the importance that they attach to making Fund surveillance more effective, particularly by focusing both global and country surveillance on the essential, sharpening the discussion of the context and of spillovers, remaining at the forefront of analysis, safeguarding the Fund's independence, and strengthening outreach. Directors agreed that the Fund remains the premier institution for global surveillance, and that it should do more to leverage its universal membership and macroeconomic expertise to achieve progress on key multilateral issues.

Directors generally welcomed the further exploration of modalities for a new consultation procedure in a multilateral format, which would allow the Fund to take up systemic issues collectively with key members as well as regional entities. A number of Directors underscored that the Board and the IMFC must be a key part of this process—as envisaged in my proposal—and that this approach must be transparent. Some Directors offered specific suggestions, as well as some qualifications, which must be considered carefully as we work out the structure and governance implications of this proposal. Directors also supported the intention to develop regional outreach and—with a view to strengthening the multilateral perspectives of bilateral surveillance—to develop new modalities for regional surveillance.

Broad support was also expressed for increased emphasis on the original objective of exchange rate surveillance, which remains to assess the consistency of exchange rate policies with national and international stability. Directors looked forward to a review of the 1977 Surveillance Decision. In this context, Directors generally welcomed management's intention to deepen the work of the Consultative Group on Exchange Rates, including by extending the scope of existing analyses of multilaterally consistent equilibrium rates to cover major

emerging market currencies. Many Directors did not support publication of equilibrium exchange rates because of market sensitivity of the information and the need to further refine analytical methods. There was a constructive exchange of views on whether exchange rate surveillance in the context of capital mobility should focus primarily on exchange rate policies, the exchange rate regime, or the exchange rate level. Directors underlined the importance of Article IV surveillance in assessing the consistency of exchange rate policies, as well as of other macroeconomic policies, with international financial stability and sustainable growth. At the same time, some Directors raised concerns about undue focus on exchange rates at the expense of other policies and their spillovers. We will need to return to these issues when we review the 1977 Surveillance Decision.

Directors strongly endorsed strengthening the Fund's two flagship publications, the WEO and the GFSR, and offered useful suggestions on the steps to enhance further their coverage and impact. I have noted the views of Directors on the proposal to produce a WEO Globalization Report, and going forward we will need to be confident that, if produced, it will add value to our two flagship publications by focusing on the implications of the forces of globalization for macroeconomic developments.

Directors welcomed the proposals in the report to make surveillance more effective. This will require raising the standard of coverage of financial sector issues, clarifying and streamlining the focus of consultations through the development of multiyear surveillance agendas, underscoring the role of the national context, and bringing to bear the multilateral perspective in bilateral consultations. Here again, Directors offered useful suggestions, including the importance of avoiding a one-size-fits-all approach to financial sector surveillance, given countries' varying situations and levels of development. In addition, Directors supported simplifying bilateral consultation procedures for a selected number of countries every other year, but in a way that ensures that members are treated fairly, and that the effectiveness of our advice on core surveillance issues is not reduced.

Directors underlined the importance of effective communication to the authorities and the broader public in explaining the policy recommendations developed in the Article IV process, and in gaining wide support for them. As some of you pointed out, in such outreach we will need to continue to be mindful of the Fund's role as confidential advisor to its members, and to work closely with the concerned authorities and Executive Directors. Also, the cost implications of such efforts will need to be assessed further.

### **Emerging Market Countries**

Directors viewed the placement of financial and capital market issues at the center of the Fund's work in emerging market countries as a key element of the Fund's strategy. The new department created from the merger of MFD and ICM will play the key analytical and catalytic role in this process, and these efforts will be supported by prioritization of the FSAP program and the Fund's work on standards and codes.

The role of the Fund in ensuring that adequate financing is available to emerging market countries covers a wide range of complex issues. These issues have been on the table for some time, but the debate on the role of the Fund over the past few months, and today's discussion, have highlighted that our strategic review provides a unique opportunity—not to be missed—to clarify the framework for Fund financing to emerging market countries in a coherent manner. The report's recommendations include: revising the guidelines on exceptional access to Fund resources outside the context of a capital account crisis; establishing flexible modalities for the duration of large-scale financing; and relying on price-based incentives to encourage early repayments. A variety of views has been expressed on whether the key challenge ahead is to modify the existing framework for exceptional access, or to apply the existing framework rigorously to any new cases, and it has also been suggested that the framework does have useful flexibility and is already working well. Many Directors supported a review of the guidelines in light of the recent experience with exceptional access.

The report has also proposed a new instrument to provide high-access contingent financing for countries that have strong macroeconomic policies, sustainable debt, and transparent reporting but still face balance sheet weaknesses and vulnerabilities. There is broad support for further work on such an instrument so that it can be properly assessed, taking into account the comments made by Directors on issues such as access, conditionality, risks to the Fund's balance sheet, and the reputational risks for both the Fund and the member. We will also continue to explore the modalities of the role that the Fund could play in judiciously supporting regional and other arrangements for pooling reserves, including by signaling sound policies, taking into account comments from Directors today.

Our discussion also covered the Fund's role in debt restructuring and lending into arrears in emerging market countries. Directors generally agreed that the orderly resolution of arrears should remain an important condition for Fund lending. They broadly endorsed the concept that financing in a debt-restructuring case should be based on an agreed medium-term fiscal envelope and a macroeconomic framework on which the Fund expresses a clear view. In addition, they agreed that greater clarity is needed on how to define the good faith criterion in light of recent experience, and in the absence of a structured debt-restructuring framework of the kind that existed in the 1980s. Directors looked forward to the forthcoming paper reviewing all aspects of the Fund's approach to lending into arrears.

### **Low-Income Countries**

In assessing the role of the Fund in low-income countries, Directors noted that two main considerations will play an important role—namely, the expected increase in aid flows, including debt relief; and the responsibility of the international community to monitor progress toward the Millennium Development Goals (MDGs)—a task in which the Fund will need to be judiciously involved within its areas of core competence.

Directors discussed how best the Fund can participate with others in assessing and monitoring aid flows in the context of the MDGs. They reviewed the principal recommendations in the report, which view Fund staff as making a contribution to the MDGs in its areas of competence by monitoring, advising, and reporting on the aggregate resource use of low-income countries, including their macroeconomic absorptive capacity. The Fund staff could perform this role effectively only by relying on other institutions with the necessary expertise—especially the multilateral development banks—in making assessments of costs of meeting the development goals and helping to mobilize the necessary funding. Based on such a partnership with these institutions, the Fund could then in principle be well placed to advise donors on the circumstances in which there is scope for more aid to be absorbed or, conversely, in which aid flows can risk macroeconomic instability.

Directors expressed a variety of views on such a role for the Fund on aid flows. Although there is broad agreement that the Fund should assess the macroeconomic impact of aid flows, many Directors expressed reservations about taking the Fund's role much beyond this—citing the limits of the Fund's mandate, the risk of mission creep, the resource-intensive nature of this work, and the extremely limited scope for finding additional resources within the Fund's budget. We should reflect on these aspects of today's discussion, exploring further the feasibility of mobilizing additional external funding for capacity building and for field-based collaboration with donors, and obtaining the necessary support from the multilateral development banks.

Directors underscored the importance of ensuring that the beneficiaries of debt relief do not again accumulate excessive debt, and called upon Fund staff to support these countries' efforts to develop a medium-term debt strategy, both in the context of Fund-supported programs, and for nonprogram countries. In addition, stronger public expenditure management systems will be needed in many countries to ensure the effective use of resources released by debt relief. Directors agreed that, while the Fund may provide technical assistance in this area, it does not have expertise in sectoral allocation assessments, which remain the responsibility of the World Bank and other institutions.

Directors considered it critical for the effectiveness of the Fund's work in low-income countries that its policy advice, support for capacity building, and financial assistance are well focused on macrocritical issues, including institutions relevant to financial stability and economic growth. Given that economic development requires an inter-disciplinary view and collective actions, clear understandings with other development partners will be crucial. Directors accordingly broadly welcomed the proposal for a country-specific division of labor between the Fund and the Bank. Following careful identification of the main growth-critical issues and the assistance required by the authorities in each low-income country, Fund and Bank staff, working with development partners and country authorities, would aim to agree on the areas in which they are prepared to take the lead, with Fund staff limiting its responsibility to those areas that fall within its macroeconomic and financial expertise. This will provide a valuable guidepost to the division of operational responsibilities between the two institutions at the country level. Some Directors considered that such a clearer delineation should yield cost savings for the Fund.

Directors considered it timely to review the modalities for Fund-Bank collaboration set out in the 1989 Concordat. They also looked forward to the recommendations of the recently-established External Review Committee on World Bank-IMF Collaboration, and to the work of the joint task force set up by the two managements.

Directors discussed the suggestion that in some cases, such as post-conflict countries, the standard of upper credit tranche conditionality may be unreasonable. The staff will explore the possibilities for a facility with a more flexible standard and a larger capacity-building component, while bearing in mind the views of a number of Directors that our current toolkit might already offer possibilities to address these issues. Most Directors supported the proposal to eliminate Joint Staff Advisory Notes in order to allow better prioritization of staff resources.

### **Governance**

Directors addressed the issues on Fund governance raised in the Managing Director's report. On quotas and voice, Directors agreed that the Fund's membership should aim for a significant step toward dealing with these issues by the time of the Annual Meetings in Singapore. A variety of views was expressed on the best way forward, with most Directors suggesting that a two-stage approach may offer the best hope for forward movement on quotas and voice. Most Directors also agreed that ad hoc quota increases for the members most underrepresented in terms of their weight in the world economy should be the centerpiece of the first stage. A broader consensus still needs to be reached, however, on how best to address other elements, including basic votes, the quota formula, and the size and composition of the Executive Board. Directors looked forward to discussion of quotas and voice at the upcoming IMFC meeting, which should provide the basis for making further progress with the aim of reaching the broadest possible consensus by the time of the Singapore meetings. Some Directors felt that such a consensus is more likely to be reached if there is a clear understanding on the elements to be included in each stage of the process. Some Directors were opposed to any ad hoc solutions in a two-stage process and preferred that the second stage be taken up immediately.

Directors acknowledged the importance of establishing an agreed transparent procedure for the selection of the Managing Director, and agreed to reflect further on the best way forward. Many Directors noted that this proposal should apply to all members of management, and be part of a broader approach covering the top management of all international financial institutions. Directors also concurred that the Executive Board must ensure that its oversight is carried out in the most effective way possible, and looked forward to coming back to this issue in the near future.

### **Capacity Building**

Directors agreed that the Fund should continue to work actively to align better its efforts to build capacity with the evolving needs of members, while addressing the constraints stemming from the growing pressures on the Fund's finances. They welcomed the

suggestions designed to establish a coherent and integrated approach combining the objectives of member countries, the expertise of functional departments, and the perspectives of area departments. Directors also welcomed the proposed leading role of the area departments in producing technical assistance strategy notes that would identify capacity-building priorities for each member and form the basis for the allocation of resources. Directors concurred that the key priorities will include the financial sector, the public finances—with a focus on revenue administration and public expenditure management—and statistics. They called on staff to explore the scope for raising additional external financing, and the feasibility and usefulness of levying charges for the use of technical assistance and training while subsidizing low-income countries. Directors broadly endorsed the suggestions for prioritization of Reports on the Observance of Standards and Codes.

### **Streamlining**

Directors discussed the wide range of suggestions to streamline procedures and reduce the flow of paper, and generally favored moving forward to implement these suggestions, including longer intervals between policy reviews; greater flexibility in ex post assessments; more selective production of selected economic issues papers and statistical appendices; greater reliance on lapse of time procedures for on-track program/post-program monitoring reviews; streamlined surveillance and program reviews; and reduced rigidities in misreporting procedures. Some Directors noted the importance of not undermining the effectiveness of ex post assessments and misreporting procedures. Staff will come back to the Board with proposed modalities requiring Board endorsement.

With regard to enhancing the effectiveness of Board discussions, some Directors pointed to the role of the Chair in facilitating full and interactive exchanges of views by Directors, and to the contribution that a more active and candid engagement by staff could make to them. Directors saw merit in reshaping the work program as a vehicle more directly linked to the implementation of the medium-term strategy, with the Board maintaining a key role in shaping the priorities and contributing to the smooth implementation of the work program without undermining management oversight.

### **Medium-Term Budget**

While Directors broadly supported the framework suggested in the medium-term strategy, they emphasized that the final decisions on priorities and implementation will have to be taken in the context of the underlying budgetary envelope. In referring to the decline of Fund income, they stressed the need to address the resulting financing gap and urged decisive actions on both the income and the expenditure sides. On the income side, they emphasized the importance of finding solutions that will place the Fund on a sound financial footing over the long term, based on stable and predictable sources of income. Directors acknowledged the contribution that an external committee, headed by an eminent personality, could make to advance efforts of the Managing Director and the Board to come to a solution that can be sustained. They noted in this context that the Board will have a key role in forging a broad consensus in this complex area. Directors noted that the priorities outlined could be

accomplished in a moderately declining medium-term budgetary framework. In this context, and while welcoming our efforts to implement the proposed strategy in a budget-neutral manner, some Directors believed that a more ambitious stance might be required, especially given the uncertainty of the outcome of the income situation. Such efforts could include the need to revisit the strategic priorities and the implementation framework of the present medium-term proposals.

### **Next steps**

The strategy paper will be circulated to the members of the IMFC, and on the basis of guidance received from the IMFC, we will prepare our next work program for Board discussion following the spring meetings. That work program will probably need to be somewhat more forward-looking than usual, given that we have enough follow-up actions that will require more than just the next six months for implementation or completion. While policy, institutional, and managerial changes flowing from the medium-term strategy will continue to shape our actions beyond the next six months, it is clear that we will be in a position to embark right away on the implementation of the strategy. This should allow us to provide a positive and substantive progress report to the governors at the Singapore Annual Meetings.