



# **International Monetary and Financial Committee**

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**Statement by Eero Heinäluoma  
Minister of Finance, Finland**

In his capacity as Chairman of the EU Council of Economic and Finance Ministers

**Statement by Minister of Finance Eero Heinäluoma, in his capacity as  
Chairman of the EU Council of Economic and Finance Ministers,  
to the IMFC Autumn 2006 meeting**

1. I submit in my capacity as Chairman of the EU Council of the Economic and Finance Ministers, this statement which focuses on: the world economy; the strategic direction of the IMF; surveillance and Fund instruments; the role of the Fund in low income countries; debt relief and development financing; and governance in the IMF.

**Economic Situation and Outlook**

2. Global economic growth remained strong in 2005 and a similar outcome is projected for 2006. Growth in North America is still robust, albeit slowing, while growth is accelerating in the EU and remains stable in Japan. The emerging Asian economies, including China and India, continue to grow strongly. Some weakening of world growth is foreseen in 2007, due to a projected slowing of US activity and the adverse impact of persistently high oil prices. Very high oil prices, and the persisting large global imbalances continue to constitute the major downside risks to global growth. Moreover, the US housing market could dampen more than expected.

3. Since the beginning of the year, the EU has returned to a robust growth path. In the first half of 2006, both the EU25 and the euro area growth rates were above potential, with growth further accelerating in the second quarter. Buoyant business and consumer confidence indicators support the positive outlook for 2006 and 2007, though subject to some downside risks. Concerning price developments, sharp increases in oil prices have brought the overall inflation in the euro area above 2%. The rising energy prices constitute a risk to medium-term price stability, although there is so far no significant evidence of a pass-through to non-energy consumer prices and wage pressure. In particular, growth in unit labour costs has been very moderate.

4. The key economic policy challenges at the current juncture include ensuring an orderly correction of the global imbalances, pursuing sound fiscal and structural policies and addressing the energy related issues. In this context:

- In light of the size and duration of the global imbalances, their orderly correction should be promoted so as to avoid potential risks to financial stability, as well as to minimise the risk of protectionist reactions. This is a shared responsibility and should be done in a way that minimizes disturbances to sustained growth. Addressing global imbalances requires determined and mutually supportive action by all parties. In particular, increased saving in the US, further exchange-rate flexibility and more domestically oriented growth in main Asian surplus economies and higher investment growth in oil-exporting countries are key in achieving an orderly adjustment. Structural reform in Europe is pursued on its own merits in order to increase potential growth and resilience to external shocks from possible global imbalances. Such reforms in the EU and Japan can also contribute to rebalancing growth and to facilitate the adjustment process.
- Moreover, substantive trade liberalisation and stronger multilateral rules, including trade facilitation and supporting sustainable development must remain a top priority in trade policy. In this respect, the EU deeply regrets the suspension of the Doha

Development Round last July. All key participants must take the necessary action to secure a successful outcome. The EU is firmly committed to play its role. We remain firmly committed to open markets, progressive trade liberalization and multilateral rules. The EU also confirms its commitment to deepen individual and collective efforts to combat piracy and counterfeiting. The Doha Development Agenda remains a central priority of our trade policy. We will continue to strive for a result that will deliver real cuts in tariffs and subsidies and will foster new trade flows, as part of a deal that should bring benefits to all WTO Members. The recent setback in the trade negotiations should not be used as an excuse for protectionist measures.

- In the EU, many Member States face important fiscal challenges, including those due to population ageing, although progress has been made towards securing more sustainable public finances, not least through pension reform. The reform of the Stability and Growth Pact emphasised the sustainability of public finances. Advantage needs to be taken of the positive economic outlook for ambitious improvements of the budgetary position. This will contribute to a better policy mix, create more room for manoeuvre in downturns and contribute to reducing debt levels significantly before the budgetary effects of ageing set in.
- The re-launched Lisbon strategy has reinforced the EU's priorities of achieving growth and employment by promoting knowledge, attracting more people into the labour market and creating more jobs. The preparation of National Reform Programmes under the revised Lisbon Agenda, and their debate in national Parliaments and with stakeholders, is an important step in that process. The structural reforms undertaken are already yielding positive results. Labour market policies, mainly focusing on the labour supply side, have contributed to increasing labour market participation. The employment rate has risen significantly since the turn of the century. Progress is also being made in improving the Internal Market's regulatory framework and in reducing administrative burdens. The EU countries are committed to further strengthening their reform efforts. In particular, the adoption of a new EU directive on services is a major step towards the deepening of the internal market.
- In the context of higher oil prices, greater threats to security of energy supply and the challenge of climate change, it is central to step up efforts to improve stability of the oil market and the global energy outlook. Europe is committed to modernise its energy policy so as to ensure increased security of supply, competitiveness of European economies, affordability of energy supply and environmental sustainability. On a global level, this requires that the energy intensity of economic activities be reduced, the share of energy supply from renewable sources be increased and sources of energy be diversified, while ensuring cost-efficient solutions. Enhancing the global energy policy dialogue between oil producing and consuming countries and the private sector remains central to improve the smooth functioning and stability of energy markets. It is important to help enhance the transparency, timeliness and reliability of demand and supply data, including through the development of a global common standard for reporting oil reserves, facilitate necessary investments in exploration, production, transportation, and refining capacity. We agree that supporting clean energy and limiting climate change are key priorities and look forward to further detailed proposals from the World Bank to leverage public and private investment into low carbon energy, energy efficiency and adaptation.

## Implementing the IMF's Medium-Term Strategy

5. At the Spring Meetings, the membership of the IMF broadly endorsed the thrust of the Managing Director's strategic review and looked forward to further work on the implementation of the proposals. EU member states welcome the steps already taken by the Fund and the intensive debate that is still ongoing on important issues.

### Quotas and voice

6. It is important that the Fund can demonstrate progress on quotas and voice. In that respect, EU member states support the Board of Governors resolution on Quotas and Voice in the IMF, and believe the two main goals to be: ensuring that the distribution of quotas adequately reflects member countries' economic weight and role in the global economy and financial system and their ability to contribute financially, as well as strengthening the voice of low-income countries.

7. We support the program of actions and the timetable set out in the Board resolution to achieve these goals, including an initial limited round of ad hoc quota increases for a small group of most clearly under-represented countries, namely China, Korea, Mexico and Turkey, and more fundamental reforms as set out in the resolution.

8. *A new quota formula.* EU members are ready to work constructively to reach an agreement on a new, simpler and more transparent quota formula as part of the second stage reflecting the purposes of the Fund. It is our view that considerations should be given to increasing the weight of GDP and openness (both in trade and in financial terms).

9. *Second round of ad hoc quota increases.* Once a new quota formula has been agreed, a second round of limited ad hoc quota increases must take place to adjust the situation of the most under-represented members. EU members must be treated equally with other under-represented members in this exercise.

10. *Future quota adjustments.* We agree that better alignment of members' quotas and their weight and role in the world economy should be considered in the context of future general reviews of quota which should be guided by Fund liquidity. We note that an established need for additional Fund liquidity is an essential precondition for any general increase in quotas.

11. *Basic votes and capacity strengthening.* We strongly support the objective of enhancing the voice and participation of low income and transition countries in the Fund. It is essential that their voting share is increased through this process. Consequently, a firm decision in Singapore to significantly increase basic votes, providing for at least a doubling, that would be implemented in line with the timetable in the resolution. We also support introducing a mechanism to safeguard the share of basic votes in total voting power. Similarly we support other options that would strengthen the voice of low-income countries, including steps to increase the number of Senior Advisors and Alternate Executive Directors of particularly large constituencies.

12. *Other governance issues.* We are ready to engage in a discussion of the appropriate selection criteria and processes for appointments of senior management in the Fund and other IFIs.

### Surveillance

13. Surveillance is part of the Fund's core mandate. In April, the International Monetary and Financial Committee set out a new approach to IMF surveillance. We welcome the continuing efforts of the Fund to take this forward. Several initiatives are underway to enhance the focus and effectiveness of surveillance. Increasing global integration means that spillovers from domestic members' policies have a greater impact today than in the past. Therefore surveillance should focus more on multilateral issues and on the spillover impact of members' macroeconomic and financial policies on other countries. The Fund should also bring its coverage of financial sector and capital market developments, particularly at the global level, at par with other core areas of expertise in surveillance.

14. The ongoing work of the Fund on the review of the 1977 Surveillance Decision can help to ensure that surveillance continues to meet the challenges of today's international monetary system. We support a revision of this Decision to create a comprehensive and consistent framework for surveillance. A revised decision should include a clear re-statement of members' obligations under Article IV. This would build more comprehensive links between the decision and the overall objectives of Article IV. The focus of IMF surveillance should be strengthened on the impact of domestic policies on external stability. We also welcome and support particular attention to the strengthening of the operational and analytical aspects of exchange rate surveillance, recognising that publication of assessment of exchange rates could raise difficult technical and market sensitive issues and needs to be considered very carefully.

15. We welcome the ongoing consultation on global imbalances. We expect that this multilateral consultation will contribute to the maintenance of the global economic expansion by providing a mechanism in which common understanding of the global imbalances issue can be strengthened and by promoting domestic policies that are mutually supportive in contributing to reduce global imbalances to sustainable level. The main target of this MC will be the implementation of the already agreed strategies notably in the context of the IMFC. We look forward to the results of this consultation to improve the design of this new ad hoc procedure, which should be appropriately embedded within the IMF's governance structure, including the appropriate involvement of the Executive Board. We will be ready to discuss themes for future multilateral consultations, in the light of the outcome of the ongoing one.

16. One of the elements of the new framework for surveillance proposed by the April IMFC was the introduction of an annual remit for both bilateral and multilateral surveillance. We support the setting of a remit for IMF surveillance to clarify medium term objectives and operational priorities of surveillance, subject to further work on the issues involved and in the context of the surveillance package as a whole. This could contribute to attaining greater focus in surveillance, enhance transparency, effectiveness and accountability, and may provide a vehicle for identifying priority issues for surveillance over the year ahead. The remit should respect the role of the Executive Board as the Fund's central body in charge of conducting the Fund's work on surveillance, as well as the role of the IMFC. We look forward to the work of the Fund after the Annual Meetings on a possible framework for assessing the effectiveness of surveillance.

## **Crisis Prevention**

17. We welcome the ongoing work of the Fund on crisis prevention, precautionary arrangements and country insurance. This illustrates how, while high quality institutions and sound macroeconomic policies are the best prevention against crisis, a program relation with the Fund can lower the likelihood of a crisis at times of heightened vulnerability. The recent experience has shown that the instrument of precautionary program can, under certain conditions, be a useful instrument to lend credibility to country authorities' policies and enhance policy discipline. We look forward to further work on the key issues in the design of a new liquidity instrument for market access countries, which would provide contingent financing for countries that have strong macroeconomic policies, sustainable debt, and transparent reporting, but which remain vulnerable to shocks. In addition, we emphasize the importance of continuing to strengthen the framework for resolving crises that do nonetheless occur, including a comprehensive review of the lending-into-arrears policy.

## **Trade**

18. We acknowledge the importance of Aid for Trade as essential in helping many developing countries benefit from trade. We reaffirm our commitment to delivering on our Aid for Trade commitments, independent of progress in the Doha Round, and call on all other donors to do the same. We welcome the reports of the Taskforces on the Integrated Framework and on Aid for Trade. We also welcome the joint work that the Fund and the Bank have done on aid for trade and we call on them to continue to strengthen their efforts to provide long-term support to countries in this area. Aid for Trade assistance should be firmly grounded in national development strategies and make full use of existing and enhanced mechanisms for trade-related technical assistance.

## **Low income countries**

19. The International Monetary and Financial Committee, on 22 April 2006, underscored the importance of ensuring debt sustainability in countries receiving debt relief. EU countries support further work on the prevention of re-accumulation of unsustainable debt by those countries. For countries on the path towards - or in the midst of - debt reduction, non-concessional borrowing should not be allowed, within the debt reduction framework. For countries that have already received HIPC and MDRI, it is necessary to prevent a rapid re-accumulation of debt, with a presumption against non-concessional borrowing supported by appropriate disincentives. For countries with a high risk of external debt distress (so-called "red light" countries), restraint should also be exercised in lending on concessional terms.

20. Since the IFIs role in monitoring debt sustainability is crucial, we welcome the review of the present Debt sustainability framework and look forward to working with the IMF and World Bank in the coming months to strengthen that framework and ensure that it is comprehensive, widely accepted and forward-looking to achieve its objective mentioned above of preventing a rapid re-accumulation of debt. We recommend that the framework incorporate measures to avoid inappropriate lending and borrowing that free rides on debt relief. These measures must reinforce ex-ante reporting obligations for debtors and address both borrower and creditor incentives.

21. Primary responsibility for prudent debt management rests with borrowing countries. Several donors are assisting countries to develop their debt management capacity and we urge

the Fund and the Bank to continue to provide technical support where this is needed. Creditor countries must lend responsibly, exercising necessary restraint in the light of the fragile financial condition of the borrowing countries. We ask for a closer creditors' coordination in the OECD and the Paris Club and in other fora in which other lenders are involved, and urge them to use the debt sustainability framework in their lending decisions. We encourage the Bank and Fund to do further work on how to contain inappropriate export promotion activity in HIPC and other low income countries from both non-OECD and OECD countries. We encourage the involvement of the private sector in these efforts. We will also be exploring how EU Development assistance could be used as an incentive to prevent new build-up of unsustainable debts.

22. We welcome the recent Board decision to let the sunset clause on the HIPC Initiative take effect, while grandfathering all countries that are assessed to have met the income and indebtedness criteria at end-2004, which will permit these countries to qualify for HIPC Initiative debt relief once they become eligible.

23. We look forward to considering the recommendations of the External Review Committee set up by the IMF and the World Bank to review the Fund-Bank collaboration. To build on progress already made, we call on the Fund and the World Bank to enhance and make more effective their cooperation and collaboration, based on a clear partnership which takes fully into account the institutions' comparative advantages, mandates and responsibilities, while avoiding gaps in response to the current challenges faced by low-incomes countries.

### **IMF financing**

24. On Fund finances, we encourage the timely implementation of the two-pronged strategy agreed by the Executive Board to address a projected income shortfall in FY 2007 and stress the need for expenditure control as well as income generation. The activation of an investment account is a welcome step in the direction of a more robust, predictable, and less volatile and credit-linked income position but more measures are needed. In light of the ongoing and projected sharp decline of the Fund's income over the medium-term, we look forward to discussing the concrete proposals of the Committee of eminent persons established by the Managing Director to make specific recommendations in early 2007 for a sustainable long-term financing of the IMF's running costs. Possible options for ensuring that the Fund has a broader, diversified and sustainable and durable income base should be presented to the Board as soon as possible.

25. On budgeting, the medium-term budgetary framework should support the IMF's strategic objectives flexibly and efficiently, with the organisation reaching for the highest standards of public sector practice in the definition and measurement of its objectives. We fully support the Fund efforts to deliver real cuts in the budget in FY 2008 and 2009. We also support an increase in transparency concerning the Fund's expenditures such that the full cost of each of the Fund's activities becomes clear. We support efforts to strengthen the Fund's risk management environment. In this area, consideration should be given to enhancing the Board's oversight role.

### **Other issues**

26. EU countries call for continued action by all countries to develop and implement strong programs against money laundering and terrorist financing according to the 40

Recommendations and the 9 Special Recommendations of the Financial Action Task Force (FATF). In order to ensure high quality and consistency of assessment reports, we encourage all assessor bodies to strengthen internal review procedures. We also encourage the IMF staff to keep providing technical assistance to, and cooperate more closely with, FATF-style regional bodies (FSRBs) to help improve their capacity to produce quality assessments. Every FSAP and OFC assessment should continue to incorporate a full AML/CFT assessment using the most recent methodology. EU countries call for assessment reports being always made public and the EU members commit themselves to do so.

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