



International Monetary and Financial Committee

Sixteenth Meeting
October 20, 2007

**Statement by Jyrki Katainen
Minister of Finance, Finland**

On behalf of Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway, Sweden

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Main messages

- *The increasingly integrated global economy highlights the need for stronger multilateral institutions. A timely and successful completion of the Medium Term Strategy is imperative to ensure that the Fund will be even better equipped to promote a stable and efficient monetary system that furthers continued economic progress.*
- *The Quota and Voice Reform must improve the legitimacy of the Fund in line with the spirit of the Singapore Resolution. The reform has to ensure a fair and adequate distribution of quotas and voice in a manner that anchors expectations about the nature and direction of future quota increases.*
- *To enhance the voice and participation of low income countries, we strongly support a tripling of basic votes and introducing a mechanism to safeguard their proportion of total voting power.*
- *The continued integration of low-income countries into the global economy presents both notable opportunities and new challenges to their macroeconomic and financial stability. The IMF plays an important role in facilitating this process through selective financing, surveillance and technical assistance in these areas. The joint review of Fund-Bank collaboration should lead to clearer division of responsibilities and closer cooperation between the two institutions.*

Introduction

1. The progressive integration in global trade and finance has carried the world economy on a robust upward trend. Now, worrying signs of its fading support are present. The protectionist sentiment is on the rise, the focus of economic cooperation is moving from multilateral towards bilateral and regional arrangements and the resolution to the Doha round of trade agreements remains elusive. At the same time, the necessity of multilateralism is underscored by other recent developments. Global solutions are needed to deal effectively with global imbalances and the risks and economic costs of climate change.
2. The international community can now convincingly demonstrate that multilateral institutions and cooperation are indeed relevant in an increasingly integrated global economy. The turbulence in financial markets underscores the importance of strong regional and multilateral surveillance, taking into account spillovers between countries as well as between financial and macroeconomic developments. Also, a timely and successful completion of the IMF's Medium Term Strategy is imperative.

Governance issues

Quotas and Voice Reform

3. A legitimate governance structure respecting the spirit of the Singapore Resolution is essential for the Fund to effectively fulfil its mission. This needs to build upon a fair distribution of quotas and votes based on a simple and transparent quota system that can stand the test of time and is based on sound economic reasoning. We reiterate our strong support for a compression factor in the formula since it is the best means of producing a balanced, transparent and rules-based distribution of calculated quotas. GDP and openness should be the main variables in the formula.
4. The allocation of the 2nd round quota increase calls for vision and far-sightedness by all involved parties. The success of the reform in the long run is not measured by a one-off adjustment in the distribution of quota and voting shares but whether we can achieve a durable solution that reduces the need for strenuous discussions on future quota increases. It is therefore imperative that the allocation of quotas and voting shares ensures fair treatment of members and quota adjustments are distributed in a manner that anchors expectations about the nature and direction of future quota increases. As a general principle, the main beneficiaries should be the most under-represented countries in relative terms according to the new formula.
5. To enhance the voice and participation of low income countries, we strongly support a tripling of basic votes and introducing a mechanism to safeguard their proportion of total voting power.
6. In order to reach the above objectives of the Quotas and Voice Reform, all should strive for a balanced compromise.

Fund finances

7. We welcome the progress made in finding a sustainable long-term model for IMF finances. Since implementation of any new model is likely to involve significant time lags, we underscore the need to move expeditiously to reach a consensus on a balanced package solution.
8. The design of the new income model should be guided by the principles of transparency, predictability, equality and cost effectiveness. The Fund must reduce its reliance on income from credit intermediation and diversify its income sources. While cross-subsidization between the Fund's activities should be minimised, rigid segmentation of the Fund's financial structure must be avoided.
9. We continue to support limited sale of gold and a prudent relaxation of the Fund's investment guidelines. However, even if such measures were to be employed, a significant deficit to the required annual financing for the Fund's non-lending activities would still be likely to remain. Other complementary measures may be needed. We encourage further analysis of the implications, technicalities and income-generating potential of the proposal to invest the Fund's quota based resources.
10. We call for continued restraint on Fund expenditures and find that further investigation on how these can be curbed is also needed. We expect preparations for taking decisions on proposals, including different compositions and substantial reduction of expenditure. The overarching objective is an appropriate balance between the tasks and re-

sources assigned to the Fund. All Fund members need to stay engaged and committed to this vital reform.

Other governance issues

11. We welcome and look forward to working closely with the new Managing Director of the Fund. We are convinced that he has the necessary background, skills and determination to lead the institution in these challenging times.
12. We consider a fully open and transparent selection process for the heads of all International Financial Institutions vital for the legitimacy of these institutions.

Fund Policies

Fund Surveillance

13. The recent adoption of the 2007 Decision on Bilateral Surveillance will make Fund surveillance more effective and transparent. Nonetheless, its real value is revealed only once the new framework is translated into more effective surveillance practices.
14. The Statement of Surveillance Priorities will strengthen the link between country-specific surveillance and the multilaterally agreed surveillance objectives. It has the potential to improve the Fund's capacity to promote transparency in global markets and prevent future crises. It can also improve the Fund's political legitimacy by enhancing external communication.
15. We continue to stress the need for increased emphasis on regional and financial sector matters in Fund surveillance. Among the primary factors underlying the global liquidity crunch has been the wide-ranging distrust between market participants caused by a lack of transparency in regard to their risk exposure. We encourage the Fund to deepen its cooperation with other international financial institutions and its membership in efforts to promote greater disclosure and transparency.
16. We encourage the IMF to investigate whether the size and investment strategies of Sovereign Wealth Funds have implications to global financial stability and the possible need for guidelines for best practices.

Low income countries

17. We are encouraged by the unprecedented period of sustained growth in low-income countries (LICs). However, the tendency to increased disparity among the LICs is a source of some concern. Many LICs now feature more prominently in global markets, not only in commodities but also in manufacturing. At the same time, their changing development dynamics, increasing exposure to external shocks and the rise in foreign exchange inflows entail new challenges to their macroeconomic and financial stability. The most fragile states are also the ones exposed to the worst consequences of climate change, which is an additional challenge for their development. The Fund plays a central role through selective financing, surveillance and technical assistance in facilitating LIC's continued integration into the global economy. Assistance in building strong institutions is especially important.
18. The Fund's work in LICs should concentrate on core areas of expertise where it has a comparative advantage. First and foremost, this means support to achieve and maintain

macroeconomic stability within the overarching objective of reaching the Millennium Development Goals (MDGs). The division of labour between the IMF and the World Bank should be clarified. This should sharpen rather than reduce the Fund's engagement in LICs. We see a need for temporary lending to these countries, but a review of the Fund's longer-term financial involvement is appropriate.

19. The Fund's role is also changing in the aid arena. The growing use of budget support by donors underlines the key role of the Fund's assessment of the LICs' macroeconomic situation. Close cooperation, coordination and communication with development partners are essential. In particular, efficient provision of Technical Assistance (TA) requires close coordination with both the recipient country authorities and with other TA-providers so as to leverage limited staffing and financial resources.
20. It is vital that donor countries deliver on their ODA promises and that aid is used efficiently in recipient countries. The expected rise in aid inflows provides an important opportunity for LICs to reach the MDGs. Using aid efficiently calls for strong fiscal institutions and prudent medium-term planning. Improvements in domestic revenue mobilization are crucial in the longer term to lessen the dependency on foreign aid.
21. We welcome the strong efforts taken to comprehensively solve the remaining protracted arrears cases. We reiterate our willingness to participate in a fair burden sharing of the costs and call for additional commitments on part of the rest of the membership. The Fund's role – in collaboration with the World Bank – in ensuring debt sustainability in these countries having benefited from debt relief is also important.