



International Monetary and Financial Committee

Thirteenth Meeting
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Statement by Honorable Tae-Shin Kwon

Vice Minister, Ministry of Finance and Economy, Korea

On behalf of Australia, Kiribati, Republic of Korea, Marshall Islands, Federated States of Micronesia, Mongolia, New Zealand, Palau, Papua New Guinea, Philippines, Samoa, Seychelles, Solomon Islands, and Vanuatu

**Statement by The Hon. Tae-Shin Kwon
On Behalf of The Hon. Duck-Soo Han, Deputy Prime Minister and Minister of Finance
and Economy of the Republic of Korea¹
to the International Monetary and Financial Committee
Washington, D.C. - April 22, 2006**

We welcome the continuing efforts to review the Fund's strategic directions and support the Managing Director's objective of maintaining the relevance of the Fund as an essential element of today's international financial environment. After a series of discussions, including the Spring and Annual Meetings last year, the medium-term strategic review is now at a stage of proposing concrete measures.

The Fund is being asked to take on too many roles and has difficulty allocating resources across competing priorities. As we emphasized at the last IMFC meeting, the Fund's core mandate should continue to be anchored to international monetary co-operation, global prosperity and financial stability. Core competencies should continue to focus on providing confidential policy advice on macroeconomic policy frameworks and associated exchange rate and financial sector regimes.

We believe this is impossible without legitimate governance of the Fund, because it determines how the Fund works. We believe it more important to be trusted by our member countries than to run the institution with technical efficiency. In this context, we are hopeful that the identified priorities, coupled with concrete actions over the near future, can lead to a Fund fully prepared to face the future with greater relevance and legitimacy.

Global Economic Outlook and Policy Challenges

The global economy in the second half of last year and early 2006 shows a continued strong and more broadly-based expansion while inflationary pressures remain subdued. We believe that the currently benign market conditions could not be expected to continue. The overshadowing risks on the downside include rising current account imbalances, high and volatile oil prices, and the potential for a tightening in financial market conditions, while risks on the upside are a gradual pickup in investment, favorable financial market conditions, and continued accommodative macroeconomic policies. To these risks, we would add the potential for a disorderly adjustment of the US housing market as a risk to the global outlook rather than merely a risk to the US outlook, given the likely spillovers.

¹ On behalf of the constituency comprising Australia, Kiribati, Korea (Republic of), Marshall Islands (Republic of the), Micronesia (Federated States of), Mongolia, New Zealand, Palau (Republic of), Papua New Guinea, Philippines, Samoa, Seychelles, Solomon Islands and Vanuatu.

While the United States is still the main engine of growth among industrial countries, it is increasingly supported by the ongoing expansion in Japan and signs of a sustained recovery in the euro area. Among emerging markets and developing countries, growth remains strong, with particularly buoyant activity in China, India, and Russia.

Against these broadly favorable developments, key vulnerabilities—most notably global current account imbalances—have still not been addressed satisfactorily. The global imbalances have widened further, particularly among the US, oil-exporting countries, a number of small industrialized countries, Japan, China, and many other emerging Asian countries. The policy challenges facing the global economy have not changed much since the IMFC met last September. To address global imbalances smoothly, we reiterate our call for more rapid implementation of the agreed policy strategy, including raising national savings in the United States—with measures to reduce the budget deficit and spur household saving; allowing currencies in surplus countries—including in parts of Asia and a number of oil producers—to appreciate; and implementing structural and other reforms to boost domestic demand in countries with large current account surpluses. We firmly believe that more decisive implementation of cooperative strategy by all major players of the global economy would lead to an effective and smooth correction of global imbalances.

Strengthening Surveillance

Surveillance is one of the core responsibilities of the Fund. We welcome continuing efforts to improve Fund surveillance and agree with the IEO's fourth recommendation in its recent report on the effectiveness of multilateral surveillance, which calls for a clarification of operational goals and better-defined operational strategies and accountabilities. In terms of operational goals, we look forward to the increased focus on exchange rate surveillance and better incorporation of financial sector issues. Improving the quality of surveillance, and leveraging from the Fund's broad membership – including through cross-country comparisons – are key to influencing policymakers who are themselves increasingly knowledgeable of global linkages and spillovers and are able to access a wide range of alternative advice.

We support the proposal to introduce multilateral consultations, but this should be on the basis of the Managing Director and senior management engaging in high-level, small group discussions with ministers and other senior officials, focused on clear objectives and attainable outcomes.

We also give full support to broadening the Consultative Group of Exchange Rates (CGER) to include systemically-important countries and to review the 1977 surveillance decision on exchange rates, as well as the increased emphasis on spillovers regional analysis and the development of forward-looking, multi-year surveillance agenda for Article IV consultations.

The proposals to strengthen the public's understanding of the Fund and the dissemination of Fund messages and advice, under a clearly-defined communications strategy, are also likely to be beneficial.

Our consistent view has been that we want better flagship publications - not more publications. Indeed, it is now time to seriously consider consolidating the WEO and GFSR into more concise documents, with an executive summary for policymakers that gives a clear, candid and integrated Fund message. We agree that the use of streamlined Article IV consultation procedures could be an effective way to target resources.

Role in Emerging Markets

We are pleased by the focus on issues surrounding the Fund's large-scale financing activities, and we stress the importance of their timely resolution in the window afforded by the current benign financial conditions. Obviously, the best form of crisis prevention will continue to be countries implementing sound policies and creating strong institutions, and for the Fund to provide well-founded, candid and feasible policy options and solutions.

The IMF also has in place mechanisms to assist countries with crisis resolution. We recognize that in the past these have not always worked effectively. We support further work being done to improve the timeliness and processes for reaching agreement on assistance, which has been a source of concern in the past. We are also supportive of the principle that conditionality should be focused on steps needed to address key vulnerabilities and to maintain a strong macroeconomic stance.

The latest proposed contingent instrument may be an improvement on the previous Contingent Credit Line in some areas, namely, speed, and it would be designed to lead on to a standard exceptional access program (should it be required) which would enable further financing with *ex post* conditionality. Key issues would seem to be finding the appropriate balance between automaticity and appropriate conditionality to safeguard the Fund's resources, and whether measures could be introduced that would reduce the starkness of "on/off signals" to the markets. Consideration could also be given to a sunset clause for such an instrument, which would allow for a trial period. We look forward to seeing further details on the proposal, including how it will overcome these inherent difficulties, before we could support the introduction of this instrument.

In our view, Article IV consultations, with the proposed increased emphasis on exchange rates and financial market issues, should be adequate for the Fund's role of "focusing on regular and intensive surveillance".

We support a review of exceptional access and consider that such a review should establish proper incentives to avoid prolonged programs of exceptional financing and to clarify the conditions for receiving such access outside of an actual capital account crisis. We therefore support incentives for early repayment based on unified surcharges that take into account credit risks based on time and the amount of exposure.

We agree that the lending into arrears policy needs to be recast to take into account 21st century circumstances. However, the Fund should continue in this new environment to uphold the promotion of early resolution of arrears and establish a clear definition of “good faith” negotiations.

Role in Low-Income Countries

As the Managing Director notes, the Fund needs to focus its activities in low-income countries tightly on its comparative advantage. It should not duplicate the activities or responsibilities of other institutions. We therefore welcome unreservedly the recently-announced external review of the delineation of responsibilities with the World Bank.

One area of concern to us is the Fund taking on the role of assessing donors’ future aid flows and adequacy for attaining the MDGs. It would seem to be unnecessary for the Fund to duplicate on aid coordination mechanisms in order to build up a complete picture of future aid flows. However, there is an ongoing role for the Fund to assess the macroeconomic impact of aid flows and this should be done as part of Article IV consultations and PRGF reporting.

We agree that there is a need for the Fund to monitor debt sustainability, including in countries that have recently benefited from debt relief through the MDRI as well as HIPC and other initiatives. We also support the design and adoption of a medium-term debt strategy for low-income countries. Importantly, the Fund should consider the conditions for re-lending under the PRGF to countries that receive a 100 percent debt write-off.

Aside from debt sustainability analysis, the Fund should also be extending its balance sheet analysis where appropriate to LICs, in order to evaluate sectoral vulnerabilities beyond the public sector, to the financial, corporate and possibly household sectors. This analysis complemented the debt sustainability analysis in the latest Article IV report on the Seychelles significantly.

We are not yet convinced of the need for another post-conflict facility. The existing Emergency Post Conflict Assistance instrument is designed to lay the foundation for medium- to long-term programs that could be supported by the Fund under the PRGF. If this is not being achieved, then there might be a need to review this instrument, rather than create another.

Quota and Governance Reform

The Fund’s credibility is dependent upon its perceived legitimacy as an international organization representative of its members. It is widely recognized that quotas have not kept pace with changes in the world economy, particularly the growth in Asian economies, and it is evident that leaving this unaddressed raises serious concerns for the Fund’s ongoing legitimacy and effectiveness. We highlight the priority of making concrete progress on quota reform before the Annual Meetings in Singapore.

We take good note of proposals in a range of fora, including the G-20, for a sequenced, two-stage approach to reform, which would involve *ad hoc* quota increases for the most under-represented countries in the near term. We consider that an *ad hoc* quota increase for the most under-represented countries should be agreed at the Annual Meetings in Singapore this year.

An *ad hoc* increase alone will be insufficient to resolve the challenges to the legitimacy and credibility of the IFIs. Comprehensive governance reform will require consideration of a range of other important issues, such as reform of basic votes; reform of the quota formula (according predominantly to economic weight) and consequential realignment of quotas; addressing the roles and responsibilities of the Executive Board; more transparent processes for senior appointments; and the size and composition of the Board. This second stage must be linked to the first to ensure more comprehensive reform, with the issues being discussed over a longer, but still defined, timeframe.

This sequenced, two-stage approach is absolutely practical and feasible. In line with this approach, we strongly believe it is now time for the membership to move beyond discussion of whether an allocation should occur to discussing which countries should receive an *ad hoc* increase, and by how much, to ensure that progress is made in time for agreement in Singapore.

We strongly propose that the IMFC delegate the Managing Director to prepare a concrete action plan for an *ad hoc* quota increase for report to the Annual Meetings in Singapore.

Capacity-Building

We emphasize that the Fund should strive to meet the technical assistance needs of its members. We welcome a leading role for area departments in preparing technical assistance notes that would identify capacity-building priorities for each member and form the basis for allocation of resources. We strongly urge the Fund to continue to take account of the unique needs of very small countries like the Pacific Island countries in our constituency.

We agree that the priority sectors for technical assistance will include the financial sector; public finance (revenue administration and public expenditure management); and statistics.

Medium-term Budget

Given the declining net income position under the current arrangements, we encourage the Fund to take action on both the expenditure and income sides of the budget. We agree with the MD's proposal to undertake an external review headed by an eminent person on increasing the Fund's income.