WORLD BANK GROUP

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT
INTERNATIONAL FINANCE CORPORATION
INTERNATIONAL DEVELOPMENT ASSOCIATION
INTERNATIONAL CENTRE FOR SETTLEMENT OF INVESTMENT DISPUTES
MULTILATERAL INVESTMENT GUARANTEE AGENCY

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Statement by the Hon. **JEAN-PIERRE ROTH,**
Governor of the Fund for **SWITZERLAND,**
at the Joint Annual Discussion

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Chairman, President Zoellick, Managing Director de Rato, Honorable Governors and distinguished Delegates, it is an honor to address you here today.

This year's Annual meetings take place against the background of the recent financial market disruptions. Unlike several financial crises of the past, the current problems have mostly affected advanced economies. An encouraging feature is that emerging market economies have escaped essentially unscathed. The consequences of these financial market difficulties for global economic growth are not fully clear yet. So far, the most likely scenario is a modest but contained slowdown. One important outcome is that market participants have started to reappraise financial risks. Even though this reassessment is in some cases painful and its consequences are not yet totally known, it is a necessary and welcome development.

So far, the international financial system has proved sufficiently resilient. However, the current events have highlighted weaknesses in the way risks are appraised not only by banks, but also by rating agencies and supervisory authorities. There is clearly scope for improvements.

> -*Banks and financial firms* need to take a broader view of risks: reputation and liquidity risks, for instance, have been underestimated. The same applies to contingent liabilities associated with new off-balance sheet financial instruments.
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> -*Rating agencies* should revisit the methods they employ to analyze credit derivatives and structured products.
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> -*Supervisory authorities* should put greater emphasis on more regular stress testing; and these tests should rely on more elaborate and diversified scenarios.

Furthermore, recent events have shown that it cannot be safely assumed that markets always remain liquid. Thus, ways have to be found to put a correct price on complex products when markets have become illiquid. While these events call for responses from both market participants and authorities, short-term activism should be avoided.

The Fund clearly has a role to play in enhancing global financial stability. We welcome the efforts to improve its financial sector surveillance activities, making them more focused, more regular, and better integrated with macroeconomic surveillance. Furthermore, Switzerland supports a possible second round of multilateral consultations on financial stability issues. It is important, though, that the Fund avoids duplicating the work of other institutions and fora. The Fund should rely upon their technical competences, but not infringe on them. A starting point for a sensible division of work could take into account the unique position the Fund is in: it is the only financial institution with a global membership.

The Annual Meetings provide a welcome opportunity to take stock of the work done by the Fund and the World Bank. At the Fund, an important project has been the revision of voice and representation. What we need is, of course, a quota formula that is at the same time simple, transparent, and in keeping with the Fund's mandate. There has been some progress. But no one could have realistically expected a smooth process in developing a new formula. In moving forward, I want to emphasize once again that, for Switzerland, the new formula and the quota adjustment must meet three principles:

> -First, GDP should be measured at market exchange rates. GDP measured in PPP terms would be a highly misleading indicator. The basic fact is that both the financial contributions to the Fund and lending by the Fund are priced at market exchange rates and not in purchasing power parity terms.
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> -Second, openness should continue to play a major role in the formula. In addition, this variable should be modernized to include financial openness. After all, the Fund's mission and its objectives make it first and foremost a monetary institution. One of its key mandates is to help safeguard international financial stability. Including financial openness in the formula would therefore give an appropriate weight to those countries with most at stake in this respect.
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> -Third, we continue to believe that the prime driver behind any general rise in quotas should be a need for increased liquidity at the Fund. Without any clear need at the current juncture, we could, at most, agree to an overall increase of ten percent.

Beyond these core principles, we are ready to work constructively towards a revised allocation of quota and voting shares to reflect the changes in the international economic environment. To this effect, Switzerland supports at least a doubling of basic votes as well as the mechanism to keep this higher share of basic votes constant in the future. The representation issue is clearly at the heart of efforts to ensure the continued relevance of the Fund today and in the future. Switzerland is ready to compromise so that an acceptable solution can be found, but we are not willing to discard the basic principles underlying the Fund's mission. I sincerely hope and indeed have great confidence that we can reach a broad consensus on this issue.

A second topic has been high on the agenda of the Fund: its new income model. New sources of income are certainly necessary, but expenditure reductions are at least as important to achieve financial soundness over the medium term. I welcome the reductions in administrative real expenditure already planned in the medium-term budget, but more ambition is warranted. We would like to see further proposals on how to control expenditures and additional efforts towards achieving greater cost efficiency. Such efforts should be accompanied by a serious discussion about the optimal size of the Fund. We would like to see an institution with a stronger focus on its core mandate: to secure macroeconomic and financial stability.

This being said, I broadly agree with the two main pillars of the new income model: first, to broaden the investment mandate of the Fund; second, to increase the amount of resources that can be invested. One way to achieve this would be a limited sale of gold. I have to admit that I feel uncomfortable with gold sales as a panacea to deal with financial difficulties. However, I could agree to a one-off and limited gold sale, with the proceeds contributing to an investment endowment. It is important, though, that any such gold sales should be handled in a way that avoids disruptions to the gold market. A second way to raise funds is to mobilize quota resources specifically for investment purposes. We consider this a promising approach, but believe that there should be an upper limit on the share of quota that can be used for this purpose. There are also equity issues to be addressed if, what is likely, not all countries would contribute.

A third important topic concerns what role the Fund should play in low-income countries. Switzerland believes that the Fund must focus its support for these members on macroeconomic stability and debt sustainability. Here it should resume its traditional role: giving advice and providing temporary balance of payments support. However, the Fund should not fill gaps in the provision of public services – such as coordinating aid flows – or in the delivery of development aid. Long-term lending should be phased out. There are other institutions more suitable to these jobs. A clear division of labor with the World Bank is essential, and we welcome the efforts currently undertaken to achieve this. Greater specialization would help increase the effectiveness of the services provided by both the Fund and the World Bank to their low-income members.

The World Bank, in a context where rapid globalization continues to create new opportunities as well as global challenges, has embarked on a reflection about its role and its mandate. We welcome President Zoellick's commitment to develop a strategy for the World Bank Group in a consultative manner with the guidance of the Board and we broadly share the general thematic orientation proposed. A sustained engagement in low-income countries, fragile states, and middle-income countries, as well as renewed efforts towards global and regional challenges and the promotion of the knowledge and learning agenda, all constitute critical areas for action.

This orientation should be further elaborated on the basis of the value added and the comparative advantage of the World Bank Group across the suggested themes. To support the prioritization process four criteria appear particularly important to us: (i) *value added and comparative advantage* of the World Bank Group, (ii) *subsidiarity*, (iii) *consistency with the Bank's core mandate* of poverty reduction and economic growth, as well as (iv) *coherence with the country-based model*.

Inclusiveness and sustainability must be acknowledged as building blocks for the long-term strategy of the Group. Moreover, good governance remains central. The recent approval of the Implementation Plan for strengthening the Bank's engagement on Governance and Anticorruption (GAC) provides a sound platform for implementing the GAC strategy, and we expect the Bank to act resolutely on this important agenda. We encourage the Board and Management to consider all opportunities and modalities for mainstreaming the issues of inclusiveness, sustainability and good governance in the Group's long term strategy.

On the themes suggested by President Zoellick, we would like to comment as follows:

First, we support the World Bank Group's commitment to play a more active role in addressing challenges and opportunities related to regional and global public goods. In our view, efforts to address global public goods should include all member countries. High income countries are affected by global challenges as well, for example in the field of climate change and communicable diseases. They can significantly benefit from the experience of the Bank. As a competent policy and technical advisor the Bank has a major role in providing assistance to all countries affected by global challenges.

We agree that climate change represents the biggest challenge on the global public goods agenda. Mitigation and adaptation to climate change will be essential to overcome poverty in many countries. The Bank has made good progress in mapping these challenges, and we welcome the activities undertaken so far under the Clean Energy Investment Framework. Further progress on the agenda will however imply to go beyond energy to address related concerns and bottlenecks in transportation, agriculture and forestry. We hence support the need for a multi-sectoral approach and we encourage the Board and Management to deepen their discussion and to review options in that matter. To secure funding, new financing windows should be envisaged with caution and only with the assurance that market distortions are avoided.

Switzerland is currently reviewing its climate change strategy and it is setting new pillars of action to reduce GHG emissions. Switzerland will continue to participate actively in the multilateral discussion related to the United Nations Framework Convention on Climate Change (UNFCCC). The current negotiations should allow to find a global consensus on a Post-Kyoto climate regime and to reduce drastically GHG emissions. We will support more actively low and middle-income countries so that they can integrate the global climate change normative framework.

Second, the Bank's engagement in low-income countries has significantly contributed to the results achieved in poverty reduction over the last decade. The country-based approach and Poverty Reduction Strategies have been instrumental in facilitating this progress. In the current context of increasing aid fragmentation, we encourage the Bank and development partners to seek further ways to strengthen the effectiveness of the country-based model, and to explore additional opportunities to promote higher growth through private sector development in low-income countries. Agriculture, business environment, trade, local financial markets and infrastructure for regional integration are areas where the World Bank Group should scale up its work. Results and performance should remain at the center of the resource allocation system in low income countries and the governance weight should remain strong.

Third, although the World Bank Group has since long been recognized as a leading contributor to the world's knowledge and learning, this domain has not yet translated into a true business line of a 'knowledge institution'. The Bank has the potential to learn from experiences worldwide and to share competences and lessons among all shareholders and stakeholders. We encourage the Bank, in the context of the long-term strategy, to reflect on the opportunities and constraints to better tap the wealth of knowledge and learning which exist in the institution and in partner countries, and to avail this to all members, borrowing and non-borrowing countries. We are convinced that the Bank may establish a dynamic and successful new business line in focused areas without crowding out service providers of the private sector.

We encourage President Zoellick to sustain efforts in finalizing the strategy rapidly; we would welcome a full-fledged discussion of the strategy by the 2008 Spring Meeting of the Development Committee.

Regarding the scaling up of aid and the role of IDA, we acknowledge and welcome progress achieved in poverty reduction, macroeconomic performance, and institution development in low-income countries, and we commend IDA for its contribution to this encouraging trend. With a strong presence at the country level worldwide, IDA is in a position to play a pivotal role in promoting coordination among partners, addressing regional and global issues, and leveraging private and public, financial and human resources. In particular, we expect IDA to support partner countries to increase domestic resources mobilization. To produce effective and sustainable development results, the quality of lending and advice is key. IDA should continue to improve the quality of these products to ensure maximum benefits to clients and to avoid re-accumulation of debt, in addition to the proposed agenda for the Bank to support scaling-up efforts.