INTERNATIONAL MONETARY FUND

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

J

Press Release No. 46

October 13, 2008

Statement by the Hon. **RUUD TREFFERS,**
Temporary Alternate Governor of the Fund and the Bank for the **KINGDOM OF THE NETHERLANDS—NETHERLANDS,**
at the Joint Annual Discussion

Statement by the Hon. Ruud Treffers,
Temporary Alternate Governor of the Fund and the Bank for the Kingdom of the Netherlands—Netherlands,
at the Joint Annual Discussion

Dear colleagues. We meet in exceptionally turbulent times, affecting all our countries one way or the other. In recent weeks we have seen that the current multilateral system has proven unable to offer a sufficient response to the complex combination of the financial, climate, food and energy crises. The world is globalized in terms of risks and opportunities, but hardly in terms of effectively responding to global crises. If every country works on a solution only for its own problems, the most vulnerable countries and groups draw the shortest draw.

We must change that, and ensure that the current response to the crises contributes to a structural change in the way we do business at the multilateral level. First, I would like to focus on the role of the International Monetary Fund as guardian of international financial stability. Subsequently I will speak about the challenges for the World Bank.

Strengthening the role of the IMF as guardian of international financial stability

The Fund can play an important role to improve the international financial architecture. A role that should be complementary to that of other international financial fora, such as the Financial Stability Forum and the Bank of International Settlements. A strengthened financial stability role of the IMF needs to be reflected in all its tasks, including surveillance, its lending framework and in its Technical Assistance.

Enhancing surveillance

The Fund has a unique position within the international financial architecture. Not only does it have an almost universal membership, it also is in active dialogue with member states through its bilateral surveillance. This dialogue goes further than just offering local authorities feedback on their policies. Indeed, the Fund's advisory role is firmly anchored in its mandate to survey macrofinancial conditions and policies in member states with the purpose to foster open economic relations and prevent negative spill-over effects. This close relationship with so many countries makes the IMF a potentially great source of knowledge on issues of local, regional and global financial stability. In order to live up to this potential, surveillance should further be tailored to assessing risks and vulnerabilities in financial sectors and markets from a macro perspective. Although the Fund has made important strides in this respect, I think there is still room for improvement.

First, the Fund can sharpen its focus on financial sector issues in bilateral surveillance and address them more systematically. Such enhanced focus requires that the IMF has sufficient financial expertise. Moreover, the statement on surveillance priorities is a step toward a more systematic approach in surveillance. A further step could include developing a framework or "checklist" of macro risks and sector specific vulnerabilities that should be assessed. I see this as a means to quickly incorporate lessons learned through the surveillance of countries and through multilateral surveillance. Moreover, a more systematic approach in surveillance can also support the implementation of policy advice of other relevant bodies, such as the FSF, and provide feedback on the adequacy of these policy responses.

But stepping up financial sector surveillance also requires the commitment from member states. The current credit crisis shows how disequilibria within and between large economies can threaten world-wide financial stability. Therefore, all systemically important economies should reach out to the Fund and sign up for an FSAP or an FSAP update.

Second, the Fund's multilateral surveillance should be aimed at identifying cross-border financial linkages and risks. The current crisis has shown how closely international financial markets and institutions are connected. Even though many of us have pointed to the risks of highly leveraged and complex financial products, none of us had foreseen the severity of the chain reactions that followed, when defaults on US subprime mortgages started to rise. We should not have the illusion that the next crisis can be predicted by the IMF or any other organisation, but we can strive to develop "early warning systems" that can at least mitigate the impact of shocks. The Fund can enhance our understanding how financial shocks ripple though the financial system and how this system interacts with the real economy.

Third, I think that financial stability considerations should also be at the forefront when the IMF is analyzing the sustainability of a country's exchange rate. Clearly, the related global imbalances have been – and continues to be - a factor in the current financial turmoil. The 2007 surveillance Decision has been an important step in redefining the Funds exchange rate surveillance and I support a firm implementation of this Decision. However, I think that from a financial stability perspective there is a difference between a potentially overvalued and undervalued exchange rate. History has shown how a sudden downward correction of the exchange rate, sometimes triggered by speculative attacks, can be the cause of a deep rooted economic crisis. Even when discounting for large methodological problems in assessing exchange rates, I think that the IMF should be very careful in its approach toward restoring equilibrium in a country with an overvalued exchange rate, both in policy advice and in communication.

Adapting the Fund lending framework

The Fund is currently reviewing its lending framework. Also in this area there might be room for better compatibility with financial stability challenges. The world-wide credit crisis reflects the vast size of cross-border capital flows and also reminds us of the importance of investor confidence, not only towards individual financial institutions, but also towards specific countries that for example have relatively large financial sectors.

Adapting the Fund's lending framework to these challenges is not easy. In a world with large capital flows, confidence could be underpinned by the possibility for the Fund to extend large amounts of financial support. This might call for an increase in access limits or the development of an insurance type of instrument. However, Fund support only works if it addresses the root causes of a crisis. This requires adequate conditionality, in order to signal a credible adjustment of economic policies. But any instrument that quickly disburses large financial packages erodes the Fund's possibility to capture appropriate policy responses. It will be a challenge to find the right balance between conditionality and access to financing. In the regard, I think the IMF should also further exploit its role as financial catalyst.

Technical assistance

This brings me to the third task of the Fund, technical assistance. In the midst of a credit crisis, it is easy to forget the important upsides of international capital flows for economic growth and prosperity. I remain fully convinced of the merits of cross-border financing. Therefore, we should help developing countries in opening-up to outside investment. Together with the World Bank, the IMF can use its technical assistance toolkit to help build institutions that are strong enough to absorb the roars of international capital markets, while benefiting from foreign investment.

World Bank: Playing the anti-cyclical role

The World Bank and other MDBs must now act to mitigate the risks of the current crises, and support the developing countries to grab available opportunities, actually helping them to sustain their growth. I appreciate the initiatives taken by President Zoellick in this regard. Over the last years, the World Bank and other MDBs have created large reserves. These reserves now can and should be used for extra financing and further mobilisation of private money flows to countercycle negative consequences for poor and vulnerable countries. And, even more than money, these countries need knowledge and top-of-the-bill, on-time advice. To deliver that, a bank has to be close to its clients. It's the local response of the World Bank that will make the difference and enable us to think out of the box.

World Bank: Linking strategy to reform on the ground

We strongly support the six strategic themes chosen as the World Bank's priorities. Now, we have to act on a translation of these priorities into the day-to-day operations of the Bank. How will the Bank change its procedures to be better able to address the challenges linked to each of the priorities?

Two examples. We definitely subscribe to the view of president Zoellick, that the Bank has an essential role to play in fragile states. His recent speech in Geneva on this topic contains a number of very interesting thoughts on this issue. But how is the Bank going to change its procedures in such a way, that it will be able to react faster to the urgent needs of fragile states in a post-conflict situation such as for example Liberia? Some progress has been made, but especially in the case of fragile states the Bank needs to be able to act firmly and swiftly in order to help materialize the peace dividend, and we as donors should support the Bank in adapting its procedures and make that possible.

Another example lies within the priority area Global Public Goods. The Netherlands welcomes the approval of the new Climate Investment Funds and the Strategic Framework on Climate Change and Development as positive first steps towards a more sustained multilateral response, within the framework of the UNFCCC. Now we need to move from theory to practice and to put both funds and the Strategic Framework into concrete action on the ground. Combating climate change and fostering development require an integrated approach in Country Assistance Strategies, and in their implementation.

World Bank: Enhancing the voice and participation of DTCs in the World Bank Group

As requested by the Development Committee during its recent Spring meeting, an initial reform package on Voice & participation has been prepared by Management, and agreed upon yesterday by the Development Committee. The Netherlands welcomes the decision to add an additional African chair to the Board and to double the basic votes, as a first step. Moreover, I am pleased with our agreement that all shareholders will uphold the principles of a merit-based, open and transparent process for selecting future Presidents of the World Bank. We simply want the best woman, or perhaps even a man for that job, irrespective of her or his passport or political affiliation.

Now, we must keep the momentum and move towards a significant realignment of shares, reflecting the global mandate of the WBG: we don't need static blocs. Shares and voting weights should therefore be determined by the relative weight of a country's economy, and also by a shareholder's use of the institution, be it through IDA donations and trust fund support or through the procurement of the WBG's financial and advisory services. That is only fair.

Accountability and effectiveness are closely intertwined. I am therefore pleased to see that the document on voice and participation pays sufficient attention to improving effectiveness through strengthening internal governance and accelerating decentralisation.

Thank you.