



THE IMF'S FINANCIAL SURVEILLANCE WORK AGENDA

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- Mandate:** The Fund has the responsibility to ensure the effective operation of the international monetary system, thereby promoting economic and financial stability and growth. The recent crisis was a reminder that these goals are best served by Fund surveillance that seeks to ensure that members' financial systems are properly regulated and supervised, and maintain the right balance between dynamism and stability.
- Motivation:** Against this background, the recent Triennial Surveillance Review (TSR) called for a report on the key elements of the Fund's strategy in this area. This call was particularly timely in view of the profound changes in the international financial landscape and policy agenda since the crisis, notably the significant multilateral commitments to financial reform and the emergence of important new global actors, such as the G-20 and the Financial Stability Board (FSB). However, articulating a fully-fledged strategy in this environment is a challenge, since the shape of the reform agenda and the institutional architecture are still evolving. Reflecting this constraint, this paper represents a stocktaking and statement of the Fund's current financial surveillance work agenda and priorities, in order to solicit input from the IMFC and other stakeholders in preparing such a strategy. It is intended, moreover, to provide a basis for the Fund to cooperate with and contribute to the work of other global actors, building on the Fund's broader mandate and membership and leveraging its comparative advantages.
- Scope:** The Fund's current financial surveillance has been strengthened considerably in recent years, shaped by two key lessons from the crisis. First, at a national level, macroeconomic policymakers and micro-prudential regulators need to expand their focus to take into account the implications of their actions for the stability of their domestic financial systems. Second, at the multilateral level, effective surveillance of the global financial system requires improved systemic risk

monitoring and enhanced cooperation. The Fund is uniquely placed to help turn these lessons into practice: it has global membership, an independent voice, extensive analytical capabilities, and well-established vehicles for macrofinancial surveillance at both the national and the global level. These comparative advantages leave the Fund well positioned to assist its members to contain the effects of the current crisis and, over the medium term, strengthen financial systems, at both the national and global levels, to remain resilient and support growth.

4. **Instruments:** The instruments for the Fund's work in this area are multi-faceted. At the bilateral level, Article IV surveillance remains the main vehicle for financial surveillance, but the Financial Sector Assessment Program (FSAP) provides the principal instrument for an in-depth assessment of systemic risks and of the robustness of regulatory, supervisory, and crisis management systems. At the multilateral level, financial sector surveillance is undertaken mainly through the Global Financial Stability Report, in an integrated manner with the World Economic Outlook, the Fund's regional surveillance documents, and through various policy papers. In addition, the Fund's vulnerability exercises are part of a broader commitment to integrate better its bilateral and multilateral surveillance. Moreover, surveillance operations have been strengthened and expanded in light of the crisis, notably through the Early Warning Exercise (EWE), thematic multi-country reports, spillover reports, and the introduction of more flexible procedures for FSAPs and the adoption of mandatory FSAPs for 25 jurisdictions with systemically important financial sectors. In addition, the Managing Director's Action Plan following the recent TSR also launched a number of initiatives to enhance the coverage of financial sector issues in surveillance (see Box). Last but not least, cooperation and joint work with other stakeholders has been intensified.

5. **Accountability:** A review of progress on all recommendations in the Managing Director's Action Plan for Surveillance will be conducted ahead of the 2012 Annual Meetings. This will include a follow up on the financial sector surveillance work agenda identified in this paper and on the broader commitment under the Triennial Surveillance Review to better integrate financial sector issues into bilateral surveillance. Moreover, as noted above, a detailed strategic plan for the Fund's work in these areas will be forthcoming, which will define the policy priorities that will emerge as the global economy exits from the crisis and the attendant resource implications and tradeoffs. This strategy will also help clarify the Fund's role in the evolving global architecture and, in particular, its relationship with the FSB once its role and legal status are clarified in light of the direction provided by the G-20.

FINANCIAL SURVEILLANCE PRIORITIES

6. The Fund's current financial surveillance work agenda has three complementary dimensions: immediate priorities related to containing the impact and spillovers of the current crisis; and medium-term priorities in two broad areas: enhancing systemic risk monitoring, and building more resilient financial systems to support growth. The forward-looking elements of this agenda build on considerable work that has already taken place within the Fund, including important policy papers on a range of topics relevant for financial sector surveillance, such as macroprudential policy frameworks, capital flow management, cross-border resolution, sovereign debt crises, too-big-to-fail, and financial subsidiarization (Tables 1 and 2). The priorities described here are intended to be delivered within the envelope of available resources and in the context of the Fund's broader surveillance priorities.

A. Immediate Priority: Containing the Current Crisis

7. In order to facilitate the recovery from the global financial crisis, the most immediate priority is to help restore financial stability, notably but not only in the euro area, and limit potential spillovers to other regions. This priority informs not only financial surveillance but also the Fund's technical assistance and lending operations.

- **Restoring financial stability in advanced economies.** In the euro area, it is essential to ensure that there is appropriate systemic liquidity, strengthened banking sectors, and an adequate firewall, complementing a comprehensive and coordinated set of supportive macroeconomic policies. These issues, as well as the need to ensure oversight of the shadow banking sector, are important in many advanced economies, not just the euro area, and are being actively pursued by the Fund across the whole range of its bilateral and multilateral surveillance activities.
- **Preventing excessive global deleveraging and improving monitoring of contagion risks.** Fund analysis is aimed at monitoring and anticipating the risks posed by excessive global deleveraging, and its policy advice—both bilaterally and multilaterally—is focused on the measures that can help contain the effects of deleveraging, including through multilateral cooperation (see recent GFSR and WEO reports). In this context, the Fund has stepped up its work on spillovers and channels of contagion across countries and asset classes (the 2012 Spillover Report will be shared with the Board in July).
- **Addressing challenges facing emerging and developing economies.** A number of emerging and developing countries are experiencing volatile capital inflows, overheating pressures,

and rising financial vulnerabilities. The Fund is actively engaged in assessing how the macroeconomic policy mix may be adjusted to face these challenges, including through applying, where appropriate, supporting macroprudential and capital flow management measures.

B. Medium-Term Priorities

8. Looking beyond the immediate challenge described above, work is ongoing on how the lessons of the crisis can be applied to improve the ability of member countries—as well as the global system as a whole—to understand better and monitor more effectively systemic risk, build more resilient and growth-enhancing financial systems, and strengthen their ability to prevent and manage crises. Many of the policy approaches discussed below are still work in progress, on which a consensus is yet to emerge. It is also clear that country circumstances are sufficiently varied so that “one size does not fit all.” Nonetheless, there are common lessons that can and should be explored further.

Enhancing Global Systemic Risk Monitoring

- **Developing a macrofinancial approach to global surveillance.** Recognizing the increased interconnectedness among countries and financial markets, there is a need for a more systemic focus, as well as a more integrated approach to macrofinancial policies, at the global level. The Fund is increasingly adopting this perspective in its own surveillance, including in its multilateral surveillance vehicles (notably in the recent GFSR and WEO), spillover reports, and work on interconnectedness, and aims at facilitating a dialogue among all relevant stakeholders on this issue.
- **Refining the analysis of interconnectedness.** The Fund is working to improve its understanding of the spillovers from highly interconnected financial centers, institutions, and markets. Ongoing refinements in the analysis of trade and financial interconnectedness will provide a more comprehensive basis for analyzing the policy implication of spillovers and contagion at the bilateral, regional, and global levels. Future analysis will focus on the policy implications of cross-border banking, fiscal-financial linkages, and financial openness.
- **Filling information gaps.** The Fund is engaged with other global stakeholders in following up on the G-20 data gaps initiative, where work is still ongoing, including with regard to strengthening sectoral and cross-border accounts and developing data templates for global systemically important financial institutions and infrastructures. Although their oversight remains with the relevant supervisory authorities, the Fund is responding to the post-crisis recognition of the risks posed by these entities by expanding its own capacity to monitor developments in this area.

- **Contributing to a framework for orderly resolution of global banks.** Domestic resolution toolkits need to be enhanced and complemented by a pragmatic framework to guide cross-border bank resolution. Earlier work by IMF staff has contributed to the development of the FSB's "Key Attributes of Effective Resolution Regimes," published in November 2011. The Fund is working now with the FSB, World Bank, and standard setters to develop a methodology to assess implementation of these measures by the end of 2013.

Distilling Country Experiences to Develop Good Practices for Resilient Financial Systems

- **Developing macroprudential approaches.** The crisis highlighted the need for a systemic and more integrated approach to macroeconomic and prudential policy making, which a number of countries are already actively pursuing. Building on their experience, as well as its own analysis, the Fund is drawing lessons that can be applied in its bilateral surveillance and technical assistance work. This involves designing better tools for identifying and monitoring systemic risk, stress testing financial systems, analyzing the costs and benefits of macroprudential instruments, and exploring alternative governance and accountability arrangements.
- **Deepening the understanding of macrofinancial linkages.** There is greater emphasis on examining national balance sheets and flows to help identify potential vulnerabilities in bilateral surveillance. Research is underway into the implications of credit cycles and real estate booms and busts on the real economy and on the appropriate responses of monetary and macroprudential policies.
- **Strengthening financial oversight.** The Fund is working in cooperation with the FSB and other standard setters to enhance global financial regulation and supervision. This involves close cooperation with the standard setters in designing revisions to the standards and the assessment methodologies. In its FSAP assessments, its bilateral surveillance, and its technical assistance, the Fund is involved in assessing and facilitating members' adherence to these international standards, but is also engaged in evaluating the impact of, and countries' readiness to adopt, the broader regulatory reform agenda, including Basel II/III requirements. Another important aspect of this work, where the Fund is uniquely well placed to contribute, is the identification of the—intended or unintended—macroeconomic consequences of this reform agenda.
- **Managing capital flows.** Work is underway to develop a balanced and flexible approach to managing capital flows to help countries reap the benefits of capital mobility while limiting the risks, and a series of papers has already been presented to the Board. The results will help the design of an approach to policies affecting capital flows, as called for by the IMFC.

- **Assessing vulnerabilities in nonbank financial institutions.** Methodologies are being developed for assessing more rigorously vulnerabilities in nonbank financial institutions and markets (such as, for example, stress testing tools for insurance). FSAPs are also increasingly focusing on the potential systemic risks springing from financial market infrastructures.
- **Promoting financial sector deepening.** The Fund is exploring the links between financial stability and economic growth and, particularly in low-income countries, the challenges and opportunities arising from financial deepening and inclusion. This goes beyond a narrow focus on banking systems' soundness and solvency and includes the role of nonbank intermediaries. Technical assistance therefore is geared toward building capacity alongside carefully sequenced liberalization.

COOPERATING WITH OTHER GLOBAL STAKEHOLDERS

9. As the Fund's interactions with its membership are mainly bilateral in nature, its main counterparts are the national authorities. Interactions with national authorities, including central banks and financial supervisory agencies, are a two-way street: they are not only the vehicle for disseminating the Fund's analysis and policy advice, but also allow the Fund to learn from the experience of its members. Beyond national authorities, however, the Fund's financial surveillance work agenda involves close collaboration with a number of global stakeholders.

- **The G-20.** The Fund works with the G-20 to assess its members' success in meeting commitments laid out in the Cannes Action Plan, including financial sector reforms (drawing on the FSB's monitoring of the implementation of agreed G-20 financial reforms) and steps to avoid disruptive deleveraging.
- **The FSB.** The Fund's and the FSB's missions have overlaps, but their approaches have thus far been complementary, leveraging their respective comparative advantages and generating important synergies. As laid out in the 2008 joint letter of the two institutions,¹ the Fund is responsible for surveillance of the global financial system and the policies of its members, and assesses macrofinancial risks and systemic vulnerabilities; while the FSB takes the lead in the elaboration of international financial sector supervisory and regulatory policies and standards and the coordination of standard setting bodies, as well as in the assessment of financial system vulnerabilities. The IMF and the FSB conduct jointly the Early Warning Exercise and collaborate on special projects on a case-by-case basis, such as the recent joint report to the G-20 on

¹ www.financialstabilityboard.org/publications/r_081113.pdf

macroprudential policy frameworks. In addition, the Fund is working with the FSB on filling data and information gaps exposed by the recent crisis and is supporting other FSB activities, such as peer reviews and the initiative to promote adherence to cooperation and information exchange standards. As a member of the FSB, the Fund brings to the table its independent and unique perspective, which reflects the interests of its entire membership.² The experience thus far has provided a solid foundation for close and effective collaboration between the FSB and the Fund, although the modalities may need to evolve in light of the G-20 call for a strengthening of the FSB's capacity, resources, and governance.

- **Standard setters.** The IMF cooperates in the development and monitoring of international standards and brings to bear the perspective of its universal membership, the FSAPs, and its general surveillance work. The Fund is itself a standard setter in such areas as data compilation and dissemination and transparency in fiscal, monetary, and financial policies. And the Fund is assessing compliance with all the core international financial sector standards through the Reports on the Observance of Standards and Codes (ROSCs), which it conducts in cooperation with the World Bank in developing and emerging market countries.
- **The World Bank.** The Fund cooperates with the World Bank in FSAPs in developing and emerging market countries—where the Bank focuses on development issues and the Fund on stability—with the ultimate goal of supporting durable economic growth and financial inclusion (FSAPs in advanced economies are carried out exclusively by the Fund). The Fund also coordinates with the Bank in providing technical assistance on financial sector issues and debt management support (through the Medium-Term Debt Strategy) in these countries.
- **Financial market participants.** Through its Financial Institutions Consultative Group and other consultative bodies, the Fund continues to engage in informal dialogue with participants in private international financial markets, including through discussions on the impact of new regulatory measures and risks to global financial stability. The Fund also seeks the views of financial market participants in the context of regular bilateral and multilateral activities.

² To this end, the Fund—like other international financial institutions—has clarified that it is not bound to support any decisions that are inconsistent with its own legal and policy framework. This is particularly important in the case of the FSB's cooperation and information exchange initiative, under which the Fund does not participate in decisions regarding the listing of non-cooperative jurisdictions and the adoption of negative measures relating to those jurisdictions that are not in accordance with the Fund's legal framework and policies.

The Managing Director's Action Plan for Surveillance: Improving the Coverage of Financial Sector Issues

The Managing Director's Action Plan for Surveillance includes a number of steps to strengthen the integration of macrofinancial linkages and financial sector issues into regular surveillance.

- **Increased use of financial sector expertise** in Article IV consultations, by assigning a financial expert to each Article IV team for countries with systemically important financial sectors (for which stability assessments under the FSAP are mandatory) and for countries with mounting financial vulnerabilities.
- **Deepening financial sector analysis in bilateral surveillance.** Internal training is being stepped up and good practices are being disseminated more widely. Cross-country lessons are being drawn from recent FSAPs. In bilateral surveillance, FSAP recommendations will be tracked systematically and progress reported regularly. Research on the implications of credit cycles and real estate boom and busts will be incorporated into regular surveillance work, and the forthcoming External Sector Reports will include an analysis of capital flows.
- **Improving the availability of financial sector information.** Availability of data remains a constraint to better macrofinancial analysis, and there is a need to ensure that financial sector data inadequacies are reported more candidly (the TSR found that only 5 reports out of 50 reported any data shortcomings in this area). The next Review of Data Provision to the Fund for Surveillance Purposes has been brought forward to 2012 to look again at this issue, among others. Separately, the Fund is cooperating with national authorities and multilateral bodies to promote better data on globally systemically important financial institutions.
- **Modernizing the legal framework.** An integrated surveillance decision, which is being discussed as a follow up to the Triennial Surveillance Review, would also clarify the importance of focusing on global economic and financial stability and would enable a focus of surveillance on non-balance of payments spillovers.
- **Adopting a financial sector surveillance strategy,** covering the objectives and instruments of the Fund's surveillance over the global financial system, countries' implementation of financial sector and macroprudential policies, and work on macro-financial linkages, as well as the relationship with other global stakeholders. The present paper is the first step toward this strategy.

Table 1. Preliminary Outline of Key Board Policy Papers

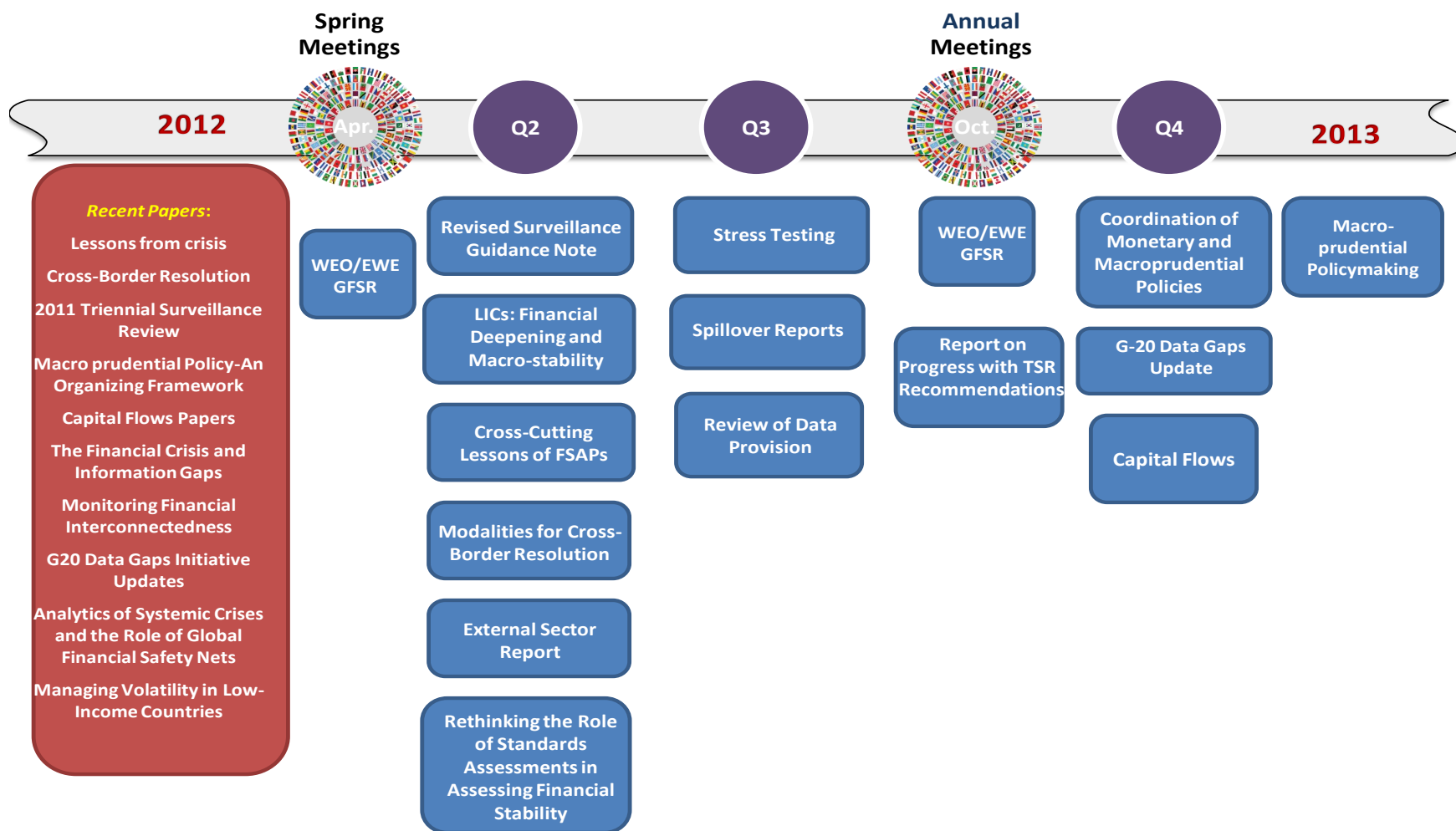


Table 2. Financial Surveillance—A Selected Bibliography of Recent IMF Policy and Other Papers

Surveillance framework and architecture

- [2011 Triennial Surveillance Review](#), October 31, 2011
- [Analytics of Systemic Crises and the Role of Global Financial Safety Nets; IMF Policy Paper; May 31, 2011](#)
- [Integrating Stability Assessments Under the Financial Sector Assessment Program into Article IV Surveillance; IMF Policy Paper; August 27, 2010](#)
- [Financial Sector Surveillance and the Mandate of the Fund; IMF Policy Paper; March 19, 2010](#)
- [The Financial Sector Assessment Program After Ten Years: Experience and Reforms for the Next Decade; IMF Policy Paper; August 28, 2009](#)

Global Financial Stability Report- Analytical Chapters

- [Long-Term Investors and Their Asset Allocation: Where Are They Now? GFSR Chapter II, October 2011](#)
- [Toward Operationalizing Macroprudential Policies: When to Act? GFSR Chapter III, September 2011](#)
- [How to Address the Systemic Part of Liquidity Risk, GFSR Chapter II, April 2011](#)
- [Housing Finance and Financial Stability—Back to Basics? GFSR Chapter III, April 2011](#)
- [Systemic Liquidity Risk: Improving the Resilience of Institutions and Markets, GFSR Chapter II, September 2010](#)
- [The Uses and Abuses of Sovereign Credit Ratings, GFSR Chapter III, September 2010](#)
- [Systemic Risk and the Redesign of Financial Regulation, GFSR Chapter II, April 2010](#)
- [Making Over-the-Counter Derivatives Safer: The Role of Central Counterparties, GFSR Chapter III, April 2010](#)

Debt issues

- [Managing Sovereign Debt and Debt Markets through a Crisis—Practical Insights and Policy Lessons; IMF Policy Paper; April 18, 2011](#)

Macroprudential policy

- [Institutional Models for Macroprudential Policy; by Erlend W. Nier, Jacek Osinski, Luis I. Jácome, and Pamela Madrid; IMF Staff Discussion Note SDN/11/18; November 1, 2011](#)
- [Macroprudential Policy: An Organizing Framework; IMF Policy Paper; March 14, 2011](#)
- [Policies for Macrofinancial Stability: Options to Deal with Real Estate Booms; by Christopher Crowe, Giovanni Dell'Ariccia, Deniz Igan, Pau Rabanal; IMF Staff Discussion Notes SDN/11/02; February 25, 2011.](#)
- [Macroprudential policy tools and frameworks Update to G20 Finance Ministers and Central Bank Governors; 14 February 2011](#)
- [Macroprudential Policy: What Instruments and How to Use Them? Lessons from Country Experiences; by C. Lim, F. Columba, A. Costa, P. Kongsamut, A. Otani, M. Saiyid, T. Wezel, and X. Wu; IMF Working Paper 11/238; October 1, 2011](#)

Capital flows

- [The Multilateral Aspects of Policies Affecting Capital Flows, SM/11/277 \(October 13, 2011\)](#)
- [The Effectiveness of Capital Controls and Prudential Policies in Managing Large Inflows; IMF Staff Discussion Notes SDN/11/14; August 5, 2011](#)
- [Managing Capital Inflows: What Tools to Use? by Jonathan D. Ostry, Atish R. Ghosh, Karl Habermeier, Luc Laeven, Marcos Chamon, Mahvash S. Qureshi, and Annamaria Kokenyne; Staff Discussion Note SDN/11/06; April 5, 2011.](#)
- [Recent Experiences in Managing Capital Inflows—Cross-Cutting Themes and Possible Policy Framework; IMF Policy Paper; February 14, 2011](#)
- [The IMF's Role Regarding Cross-Border Capital Flows; IMF Policy Paper; November 15, 2010](#)

- [Capital Inflows: The Role of Controls; by Jonathan D. Ostry, Atish R. Ghosh, Karl Habermeier, Marcos Chamon, Mahvash S. Qureshi, and Dennis B.S. Reinhardt; IMF Staff Position Note SPN/10/04; February 19, 2010](#)

Global regulatory reform agenda

- [Report on the Group of Twenty Finance Ministers and Central Bank Governors on Financial Stability Issues in Emerging Market and Developing Economics \(EMDE\), November 3, 2011.](#)
- [Managing Volatility in Low-Income Countries: The Role and Potential for Contingent Financial Instruments; IMF Policy Paper; October 31, 2011.](#)
- [The Too-Important-to-Fail Conundrum: Impossible to Ignore and Difficult to Resolve; By Inci Ötker-Robe, Aditya Narain, Anna Ilyina, and Jay Surti and al.; IMF Staff Discussion Notes SDN/11/12; May 27, 2011.](#)
- [Subsidiaries or Branches: Does One Size Fit All? by Jonathan Fiechter, Inci Ötker-Robe, Anna Ilyina, Michael Hsu, André Santos, and Jay Surti; IMF Staff Discussion Notes SDN/11/04; March 7, 2011](#)
- [Impact of Regulatory Reforms on Large and Complex Financial Institutions; IMF Staff Position Note SPN/10/16; November 3, 2010.](#)
- [Shaping the New Financial System; by José Viñals, Jonathan Fiechter, Ceyla Pazarbasioglu, Laura Kodres, Aditya Narain, and Marina Moretti; IMF Staff Position Note SPN/10/15; October 3, 2010.](#)
- [Redesigning the Contours of the Future Financial System; by Laura Kodres and Aditya Narain; IMF Staff Position Note SPN/10/10; August 16, 2010.](#)
- [A Fair and Substantial Contribution by the Financial Sector, G-20 Toronto Summit, Toronto, Canada, June 26-27, 2010](#)
- [The Making of Good Supervision: Learning to Say “No”; by Jose Viñals and Jonathan Fiechter with Aditya Narain, Jennifer Elliott, Ian Tower, Pierluigi Bologna, and Michael Hsu; IMF Staff Position Note SPN/10/08; May 18, 2010](#)

Crisis management

- [Crisis Management and Resolution: Early Lessons from the Financial Crisis; by Stijn Claessens, Ceyla Pazarbasioglu, Luc Laeven, Marc Dobler, Fabian Valencia, Oana Nedelescu, and Katharine Seal; IMF Staff Discussion Notes SDN/11/05; March 9, 2011](#)
- [Resolution of Cross-Border Banks—A Proposed Framework for Enhanced Coordination; IMF Policy Paper; June 11, 2010](#)
- [Exiting from Crisis Intervention Policies; IMF Policy Paper; February 4, 2010](#)
- [Crisis-Related Measures in the Financial System and Sovereign Balance Sheet Risks; July 31, 2009](#)

Interconnectedness and data gaps

- [The Financial Crisis and Information Gaps, Implementation Progress Report, Prepared by the IMF Staff and the FSB Secretariat, June 2011](#)
- [Understanding Financial Interconnectedness - Prepared by the IMF's Strategy, Policy, and Review Department and the Monetary and Capital Markets Department, in collaboration with the Statistics Department and in consultation with other Departments, October 4, 2010](#)
- [The Financial Crisis and Information Gaps-Progress Report, Action Plans and Timetables; Prepared by the IMF Staff and the FSB Secretariat, May 2010](#)
- [The Financial Crisis and Information Gaps: Report to the G-20 Finance Ministers and Central Bank Governors; Prepared by the IMF Staff and the FSB Secretariat October 29, 2009](#)