

SHARE WORLD SEMINAR 2008

A Changing World: Setting New Rules

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Hand in Hand: IMF Collaboration with Developing Countries in the Financial Crisis

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¹ The views expressed in this presentation are those of the author and should not be attributed to the IMF, its Executive Board, or its management.

Overview

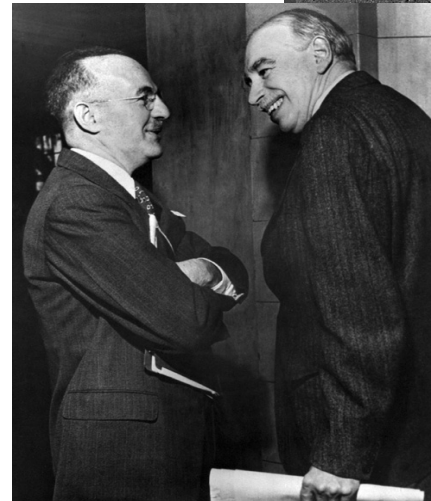
- Introduction/background on IMF
- Global financial crisis: origins, policy response, implications
- How the IMF is helping
- Next steps in reform of “global financial architecture”

Introduction

- **IMF, World Bank:** specialized agencies of UN system; total UN staff: 64,700 (IMF: $\pm 2,500$; WB: $\pm 10,000$).
- **Mandates:** promote stability of the international financial system (IMF); promote economic development (WB).

Why the Bretton Woods System Was Created

- **Avoid Past Mistakes -**
Disastrous economic policies that contributed to Great Depression of the 1930s and WW II
 - *Protectionism*
 - *Tariff wars*
 - *Competitive Devaluations*
- **Rebuild confidence in international cooperation and international financial system**



Roles of IMF and World Bank

IMF



World Bank



- Promote global financial stability
- Exchange rate stability (balanced growth of trade)
- Forum for international monetary cooperation
- Temporary financial assistance to members experiencing balance of payments difficulties

- Reconstruction and economic development after WWII
- Long-term economic development
- Project financing, including infrastructure, energy, education, health

Who Governs the IMF?

- IMF governed by member countries, through Board of Governors (1 governor per country). Meets annually.
- Subset of governors--International Monetary and Financial Committee (IMFC)-- advises Board of Governors. Meets 2 x year.

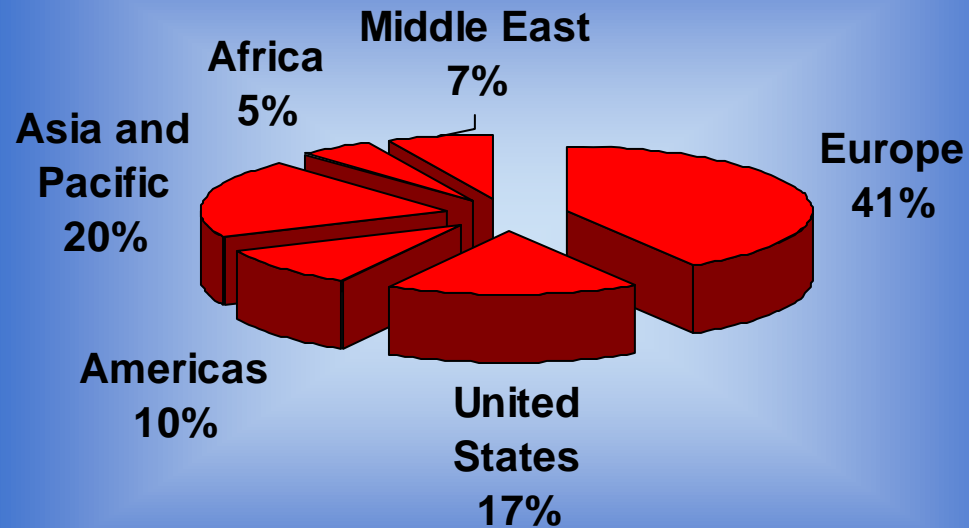
Funding, Quotas, Voting Power

- IMF capital base consists of membership **quotas**: the financial contributions made by member countries. Total quotas nearly \$300 billion.
- Quotas broadly determined by their **economic position** relative to other countries, and reviewed regularly.
- A country's quota determines its **voting power** and **access to financing**.

Reforms to increase share of developing countries

- Quotas raised for **China**, Turkey, Korea, Mexico in 2006.
- April 2008 approved:
 - further increase in quota/votes for mainly developing countries (including **China**)
 - formula more closely based on GDP
 - regular 5-yearly reviews
- Awaiting approval from countries.

Distribution of quotas



IMF: 3 main functions

- **Surveillance: (economic analysis/advice):** appraise each member's exchange rate policies within overall analysis of general economic situation.
 - **Multilateral:** World/Regional Economic Outlooks; Global Financial Stability Report;
 - **Bilateral:** Annual assessment (Article IV consultation); financial sector (FSAP); standards and codes.
- **Financial assistance:** loans to support countries with BoP problems and **low income countries** (concessional loans, Policy Support Instrument, external shocks facility (ESF)).
- **Technical assistance:** advice/support on technical issues related to macroeconomic policy.

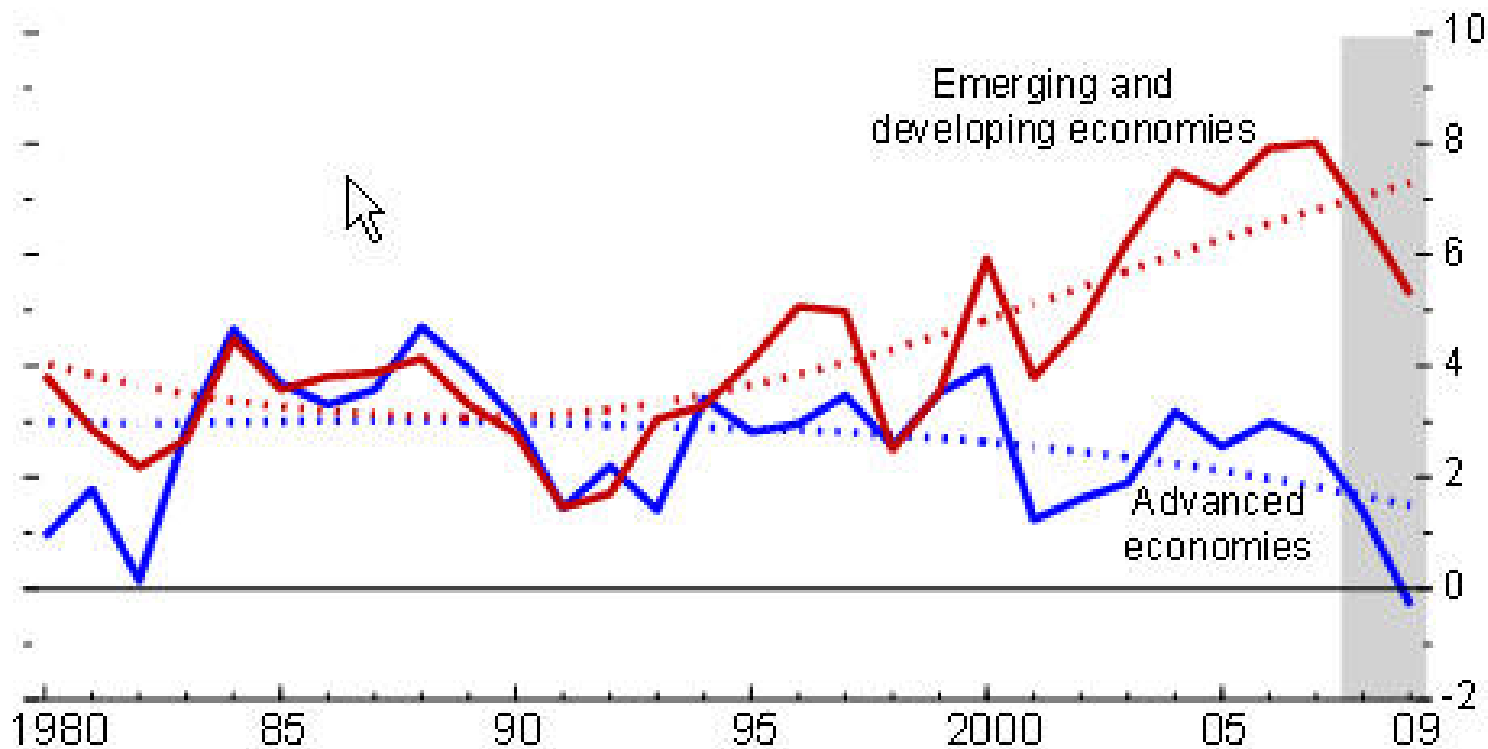
Global financial crisis

- Financial turmoil: loose monetary policy and regulation led to excessive leverage and risk.
- “Sub-prime” problem sparked off financial turmoil, leading to world recession.

World economy slowing sharply

Figure 1. Real GDP Growth and Trend

(Percent change)



Source: IMF staff estimates.

Led by advanced economies, but EMs also affected (e.g., deleveraging, ↓ export demand)

GDP growth (in percent)
(WEO Update - November)

	2008	2009
World	3.7	2.2
Advanced economies	1.4	-0.3
United States	1.4	-0.7
Euro area	1.2	-0.5
Japan	0.5	-0.2
Emerging and developing economies	6.6	5.1

Global financial crisis: origins and policy responses

- **Outline of crisis:**
 - monetary policy and easy regulation spurred risk taking and leverage,
 - supervision/regulation failed to keep pace with financial innovation.
- **Responses:** focus on *financial sector* (liquidity; recapitalization; distressed assets) and on *economic stimulus*.

How is current crisis similar/different from the Asian crisis (1997-1998)?

- Financial crisis (U.S.) versus financial-plus-f.x. crisis (Asia): different implications for **monetary policy**
- **Fiscal policy** easing: similar response
- **Financial sector**: similar responses: early loss recognition; liquidity support; support depositors; close non-viable institutions; AMCs; bank supervision
- **Trade/capital** liberalization: situations different; also, advice more focused.

Role of Fund

- **Early warning signs** (WEO: danger of “disorderly adjustment”; GFSR April 2007: risks in sub-prime)
- **Financial assistance**, including via a new facility
- **Policy advice**
- **Multilateral assessments**, distilling international experience

Actions and issues

- **Moving quickly to help affected developing countries.** Hungary; Iceland; Pakistan; Ukraine.
- **Stand ready to do more.** Offering policy advice.
- **New short-term liquidity facility:** help countries with sound fundamentals that face acute liquidity pressures. Fast/flexible, no conditionality.
- **Questions of resources and new roles** in global financial architecture. (November 15 summit.)

Surveillance guided by priorities

Economic priorities

- Resolve financial market distress
- Strengthen global financial system
- Adjust to sharp swings in commodity prices
- Orderly reduction of global imbalances

Operational priorities

- Risk assessment
- Financial sector and real-financial linkages
- Multilateral perspective
- Exchange rates and external stability risks

Next steps

- **“New Bretton Woods”?** Foundations need to be carefully laid. November 15 summit welcome.
- **Immediate tasks and longer-term issues** in global financial architecture include:
 - Dealing with **fall-out from crisis** (coordinating responses, providing financial support)
 - Ensuring adequate **resources** for the Fund
 - Fixing the inadequate **regulatory system**
 - Developing a reliable **early warning system**
- Ongoing need: strengthen **voice and representation** of under-represented countries, including China.

Looking forward: 2 main challenges

- Restore economic and financial stability
- Reform global financial “architecture” to make global economy calmer, less prone to instability

Immediate concerns

- Financial markets: to get credit flowing again
- Fiscal measures: offset fall in private demand
- Liquidity support for developing countries

The IMF can help by:

- Monitoring **global economy/markets** and providing timely advice on **risks**
- Help finance ministries to design and implement effective **fiscal stimulus**
- Help **emerging economies** design good economic programs and provide enough finance to support them

Policies to avoid future crisis

- Changes in financial market regulation (oversight)
- International coordination (role of international institutions (IMF, FSF, etc.))
- IMF: at corner of Wall St./Main St.
- Early warning systems

Representation

- G20 increasingly important. More voice for major emerging countries
- But multilateral institutions important voice for all countries, including non-G20
- And Fund working to increase role of emerging countries (quota, vote, voice)

Conclusion

What really matters is to:

“make a useful contribution” and “help build a world based more on humanity and cooperation”