The International Community's Response to the Economic and Financial Crisis and its Impact on Development

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I. Introduction

The dramatic economic and financial strains that first emerged in 2007 represent an unprecedented global challenge, and have elicited an unprecedented and cooperative global response. While the global growth downturn has not yet been reversed, and financial sector functionality has not been restored fully, it is expected that the unprecedented anti-crisis policy efforts already underway will produce substantial progress in the coming year. Nonetheless, downside risks to this outcome remain notable, while significant new efforts also will be required to correct the systemic flaws that produced the preconditions for the current crisis. Thus, new international efforts will be essential for achieving a sustainable and balanced global growth rebound.

This note presents an overview of the IMF's analysis of the causes of the crisis and the priorities for new policy initiatives. In addition, it describes the IMF's own efforts to respond quickly and effectively to its members' needs. It also discusses some of the longer-term reforms required to strengthen the global economy, and to ensure more effective global governance arrangements.

II. Key Factors Behind the Crisis

The IMF has analyzed extensively the causes of the crisis. At its root, the crisis is the result of a serious market failure – reflecting excessive investor optimism after an extended period of strong growth, low market volatility and low real interest rates – compounded by a series of key policy and regulatory failures.

- ***Financial regulation.*** The perimeter of regulation was poorly drawn in most countries, leaving large risk concentrations and leverage buildups out of regulators' sight. Financial supervisors were preoccupied with the formal banking sector, not with the risks building in the shadow financial system. At the same time, critical microprudential issues, such as overall leverage, and macroprudential aspects, such as the impact of the economic cycle on systemic risks, were ignored.

- ***Excessive risk taking by the private sector.*** Market discipline failed as optimism prevailed, due diligence was outsourced to credit rating agencies, and a financial sector compensation system based on short-term profits reinforced the momentum for risk taking. Some unregulated companies and vehicles, for example, were able to assume both credit risks and significant liquidity risks.

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[1] Prepared by Staff of the Strategy, Policy and Review Department.

- ***Macroeconomic policies.*** Unprecedented global imbalances, currency misalignments and record buildups of international reserves were all warning signs of potentially unsustainable inconsistencies in national macroeconomic policy choices. While needed policy shifts were specified in detail in the 2006/07 IMF-sponsored Multilateral Consultations on Global Imbalances, the agreed initiatives in general were not implemented as planned.

- ***Global architecture.*** Three gaps remain to be filled: First, gaps in information, where the lack of market transparency may lead to faulty decisions. Second, gaps in regulations that create systemic fragility. Third, gaps in markets that force policymakers to self-insure against systemic fragility. Filling these gaps will call for new forms of international cooperation.

III. Policy Response Needed

The IMF believes that a comprehensive approach to restoring public confidence in the financial sector and re-launching global economic growth is essential.

- To get the global economy moving again, governments, central banks, and regulators must act decisively to restore confidence in financial institutions. Much has been done in this respect, but policymakers must deal more decisively with distressed assets and recapitalize weak but viable institutions.

- Monetary policymakers have used both conventional and unconventional measures to ease credit conditions. However, given the impaired conditions of the financial system, monetary policy alone will not be able to offset financial market disruption and the severity of the downturn.

- Fiscal stimulus is needed across countries with fiscal space, with temporary and targeted measures on both the revenue and expenditure sides designed to address the core problem of slowing demand. The IMF has recommended 2 percent of GDP stimulus at the global level, and a concerted stimulus effort among several countries is already underway. This needs to be sustained in 2009 and 2010. However, policymakers should not lose sight of the importance of medium- and long-term fiscal sustainability, and should announce now plans to be implemented later.

- Many countries do not have sufficient fiscal space to implement expansionary fiscal measures in a sustainable way. In particular, many low-income and emerging market countries, but also some advanced countries, face additional constraints such as volatile capital flows, high public and foreign indebtedness, and large risk premia. The fact that some countries cannot engage in fiscal stimulus without external assistance makes it all the more important that others, including some large emerging economies, do their part. The Fund has been providing finance to allow some of them to contract less than otherwise would be the case.

- Many of the world's poorest countries will require additional external support to safeguard their hard-won economic gains as they are being severely affected by the global crisis. With export and fiscal revenues declining sharply and private financing sources drying up, stepped-up external assistance will be critical for protecting vital social and MDG-related spending and avoiding a forced pro-cyclical adjustment.

- There is broad consensus on the need to avoid protectionism in all forms in implementing policy responses to the crisis. Generally, a more open and secure international trading system would be a critical element of the future economic order. Achieving an ambitious and development-oriented conclusion to the Doha Round is essential. Moreover, more stable arrangements for trade financing that preclude the types of disruptions observed over the past few months would be critical. Donors should step up their efforts in providing Aid for Trade to low-income countries, to enable them to take full advantage of trade as an engine for recovery and sustainable growth. Protectionism in financial markets, including over the provision of foreign direct investment, must likewise be avoided. Financial support packages should not include measures that artificially favor domestic lending or other activities.

Moving beyond the immediate policy response, fiscal and monetary policies that are put in place to relaunch economic activity and overcome the liquidity and credit crunch should be formulated with a medium-term perspective, with a view to their sustainability after the crisis. Exit strategies to unwind stimulus measures as conditions return to normal need to be designed today.

Monetary Policy

Monetary policy will eventually have to move out of crisis mode. There should be a proper planning of a timely and orderly exit from ad-hoc measures and the exceptional use of unconventional instruments ("quantitative easing" and the like). As the regular instruments of open-market operations regain their former importance, the infrastructure underlying traditional open-market operations should be strengthened. The careful unwinding of the huge expansion of the balance sheets of some central banks due to the crisis should commence as the private sector re-engages.

Going forward, the capacity of central banks to provide liquidity and respond to systemic shocks should be strengthened through ongoing powers to use a wider range of instruments as appropriate. More generally, the capacity of national authorities to respond to systemic crises should be improved by establishing mechanisms for coordination among policymakers and regulators, both within and across borders.

Central banks' mandate should include macro-financial stability, not just price stability. The framework for policy decisions should assess the longer-term implications for inflation and economic growth of asset price trends, credit booms, leverage and the accumulation of systemic risk. This approach would require the careful monitoring of systemic risk—including new measures, such as potentially unsustainable growth of credit, system-wide leverage, over-reliance on short-term wholesale funding, foreign exchange exposure and the like.

To be effective in the context of globalized financial markets, national monetary policy must be complemented by comprehensive prudential and supervisory policies that can help reduce systemic risks. Closer international coordination of these measures is needed to avoid regulatory arbitrage and ensure effectiveness (see below).

Fiscal Policy

A significant fiscal stimulus is needed to respond to the ongoing crisis, where country-specific circumstances allow. The stimulus should be large, targeted and temporary, to address the magnitude and likely duration of the crisis, but also recognize the paramount need for fiscal sustainability. Fiscal stimulus should rely primarily on spending measures, given the possibility that the beneficiaries of tax cuts might save the proceeds. The focus of expenditure increases in advanced economies should be on goods and services, because the first-round effects of these increases are more certain. While the operation of automatic stabilizers in advanced countries could be sufficient to mitigate the impact of the crisis on the poor, additional discretionary measures could be needed in LICs with weak social safety nets. To minimize the risks to fiscal solvency, governments should plan their exit strategies carefully and signal their commitment to prudent fiscal policy early on. Although the stimulus should be lasting, it must be withdrawn when conditions permit.

The collective approach taken to providing fiscal stimulus enhances the effectiveness of actions taken by individual countries. For instance, without coordination, countries with a high degree of trade openness may implement sub-optimal stimulus because some of the benefits of the stimulus would leak to trading partners.

IV. The IMF's Response

As the world economy has become engulfed in the crisis, the IMF has mobilized on many fronts to support its member countries—increasing its lending, using its cross-country experience to advise on policy solutions and provide technical assistance, and introducing reforms to modernize its operations and become more responsive to member countries' needs. In recent meetings of world leaders and finance ministers—including the G-20 and the IMFC—the IMF's role in helping to combat the global economic crisis and reinforce the financial system going forward was reaffirmed.

The IMF has been strengthening its approach and role in a variety of ways:

- ***Economic forecaster.*** IMF economic forecasts are a central reference point for member countries and for the G-20 in its new enhanced role as it responds to the crisis.

- ***Policy advisor.*** The IMF is playing a critical role in assessing with governments the impact of the crisis and discussing appropriate policy responses, including a stronger role as the provider of financial sector policy advice.

- ***Economic surveillance***. The IMF will monitor policy implementation by governments around the world and has been asked to beef up its early warning exercise, jointly with the Financial Stability Board. In doing so, it will draw on its unique capacity to analyze the relationships between financial markets and the real economy, with a global perspective given its membership. Its global and country surveillance procedures are being sharpened (see below).

- ***Lending***. The IMF has responded quickly to the global economic crisis, with lending commitments reaching a record level of over \$158 billion, including a sharp increase in concessional lending to the world's poorest nations.

- ***Contributing to strengthening the international financial architecture***. The IMF is contributing to the ongoing effort to draw lessons from the crisis for policy, regulation, and reform of the global financial architecture.

A. Stepped-up Crisis Lending and Greater Flexibility

The IMF has moved swiftly to respond to the varying needs of its membership in this global crisis, with lending commitments now reaching a record level of over \$158 billion.[2] This includes a sharp increase in concessional lending to the world's poorest nations. New financing arrangements, or augmentations of existing arrangements have been rapidly approved as needed to provide countries with necessary resources in responding to the crisis.

In parallel, the IMF has also overhauled its general lending framework to make it better suited to country needs and to further streamline the conditions attached to loans. One objective of the lending overhaul is to encourage countries to come to the IMF as early as possible, including in a precautionary fashion, rather than when their problems have become intractable. Key elements of the lending overhaul include:

- ***Doubling member countries' access to resources.*** The IMF is offering higher amounts and tailoring loan terms to countries' varying strengths and circumstances. The amounts normally available under the various lending facilities (normal access limits) have been doubled, as have the cumulative limits on country debt to the IMF. These higher limits give confidence to member countries and financial markets that adequate resources will be available to the countries to meet their financing needs.

- ***Quick disbursing facilities that aim to reduce the stigma of borrowing.*** A new Flexible Credit Line (FCL) for strong-performing economies has been introduced, to provide large and upfront financing to members that meet strict qualification criteria, including having very strong fundamentals and policies. As the FCL is not tied to specific policy goals agreed with the country, there are no conditions to meet once a country has been approved for the FCL, and it can be used as either a contingent (precautionary) credit line or to meet actual balance of payments needs.[3] Countries that may not qualify for the FCL

[2] This includes recent requests under the new Flexible Credit Line (FCL). It represents a very quick ramping up relative to a low of \$14 billion at end-2007, as well as a much larger scale than in recent years. For example, total IMF loans committed in the peak years of 1998 and 2002 were \$86.2 billion and \$87.9 billion, respectively.

[3] As of end-May, 2009, Colombia, Mexico, and Poland had requested and been approved for access to the FCL totaling \$78 billion. The use of the FCL in these cases was well received by markets.

but need similar insurance can count on front-loaded high-access precautionary arrangements, known as High Access Precautionary Stand-By Arrangements (HAPAs), as a regular lending window. Like the FCL, HAPAs can be frontloaded based on the strength of a country's policies and the external environment.

- ***Elimination of "hard" structural conditionality,*** with greater focus on achieving the objectives of policies, rather than on implementing specific actions. Following up on ongoing efforts since 2002 to rationalize and streamline the practice of conditionality, the IMF has recently taken further steps aimed at ensuring that conditions linked to IMF loan disbursements are tightly focused and adequately tailored to the specific circumstances of members. Starting May 1, 2009, structural performance criteria were discontinued for all IMF loans, including for programs with low-income countries. Structural reforms will continue to be part of IMF- supported programs, but only when they are seen as critical to a country's recovery; and the monitoring of these policies will be done in a way that reduces stigma, because countries will no longer need formal waivers if they fail to implement an agreed measure by a specific date.

- ***More flexibility, fewer conditions***. IMF-supported programs have been tailored to individual country circumstances and focus on the most immediate issues to resolve the crisis.[4]

- ***Emphasis on social protection*****.** Across all programs, the IMF is committed to supporting the protection of the poorest and most vulnerable. The IMF tries to ensure that economic adjustments taken to combat the impact of the crisis also take account of the needs of the most vulnerable by developing or enhancing social safety nets. Social spending is being preserved or increased wherever possible, and about a third of programs in low-income countries include floors on social and other priority spending. The more recent programs in other countries affected by the crisis explicitly provide for higher social spending, strengthening social safety nets, and better targeting of existing systems.[5] The IMF is working closely with the World Bank and donors to identify external financing for social protection and promote social safety net reform.

B. Responding to the Needs of Low-Income Countries.

The IMF is reforming its lending framework for low-income countries to ensure that the spillovers from the global crisis do not roll back these countries' previously hard-won gains on macroeconomic stability and poverty reduction. Key steps taken or envisaged include:

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[4] For example, the September 2008 IMF-supported program in Costa Rica uses expansionary fiscal policy to mitigate the adverse effects of the drop in private demand during 2009, including increases in the wage bill and infrastructure spending. The April 2008 IMF-supported program in Guatemala seeks a moderate fiscal stimulus to support domestic demand, financed by substantial external resources from multilateral institutions, and includes a refocusing of public expenditures towards social spending and labor-intensive public works.
[5] See Factsheet on "The IMF's Role in Helping Protect the Most Vulnerable in the Global Crisis", May 2009, http://www.imf.org/external/np/exr/facts/protect.htm.

- ***Significant increase in concessional lending.*** To help meet the extra financing needs that the response to the crisis requires, the IMF plans to scale up its concessional financing substantially in 2009-10—at least doubling the concessional lending over the next 2-3 years. To this end, access limits and norms have already been doubled for the Poverty Reduction and Growth Facility (PRGF) and the Exogenous Shocks Facility (ESF).

- ***Factoring in more flexibility on fiscal policy and inflation.*** Wherever possible, the IMF encourages fiscal stimulus in low-income countries during the recession. LICs with output gaps and sustainable debt and financing options have scope to implement expansionary policies. The main focus of fiscal stimulus in LICs should be on infrastructure and social spending, given pressing needs. Some countries may have to adjust, but in a way that does not affect critical spending. The need for adjustment in the latter countries can be mitigated if adequate donor financing is available.[6] The IMF has generally advised higher deficits and spending in 2009, and has made financial assistance programs more flexible. Fiscal targets have been loosened in close to 80 percent (18 out of 23) of African countries that have an active IMF-supported program, so that government spending can be preserved or increased during the downturn.[7] Similarly, the inflation objectives in programs with low-income countries were substantially relaxed during 2008, as world food and fuel prices rose, to avoid an unwarranted compression in real spending.

- ***Streamlined loan conditions.*** As noted above, for all countries, including low-income countries, structural conditionality is now more tightly focused on core objectives and will no longer be set as performance criteria. The number of structural conditions has decreased in many programs, and has been increasingly limited to the most critical measures, in particular urgent public financial management reforms.

- ***Facilities will be reformed to provide more options to low-income countries.*** The IMF is also reviewing its toolkit of instruments for low-income countries with a view to introducing more flexible short-term, precautionary, and emergency financial assistance.

- ***Continued progress on debt relief initiatives, while reviewing debt limits and the debt sustainability framework.*** As of May 2009, 24 low-income countries have received debt relief from the IMF through the Heavily Indebted Poor Countries (HIPC) and Multilateral Debt Reduction (MDRI) initiatives totaling about $6 billion; and others are being helped to make progress. As part of a broader review of the debt sustainability framework being undertaken by the IMF and World Bank, the IMF is also reviewing its policy on external debt limits in programs, to allow for more flexible borrowing strategies in countries with strong macroeconomic and debt management capacity.

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[6] See "Fiscal Policy in Sub-Saharan Africa in Response to the Impact of the Global Crisis", IMF Staff Position Note /09/10, May 2009.
[7] On average for all sub-Saharan Africa, fiscal deficits are being widened by 2 percent of GDP in 2009.

- ***Expanded provision of technical assistance***. The global financial crisis has also increased demand for IMF policy advice and technical assistance, which have proven critical in the IMF's support to low-income countries. With the help of its development partners, the IMF will expand the delivery of capacity-building technical assistance in Sub-Saharan Africa, Central Asia, and countries in Central America and the Caribbean by establishing four more regional technical assistance centers (RTACs). The work of the RTACs will be complemented by globally operating multi-donor trust funds providing specialized assistance in the Fund's core areas of expertise.

The IMF continues to advocate scaled-up donor support under favorable terms. IMF financing covers only around two percent of low-income countries' (gross) external financing needs, so ensuring adequate levels of financial support on terms consistent with debt sustainability depends above all on the responses of bilateral donors and the multilateral development banks. Working with recipient countries, the IMF seeks to ensure that the overall financing terms they receive under IMF-supported programs are appropriate to their situations and to securing debt-sustainability.

C. Boosting IMF Resources and World Liquidity

Going forward, it is important that the IMF has sufficient resources to meet the needs of members, even if the crisis continues to deepen. After the immediate impact of the financial crisis on advanced countries, and its spread to emerging market economics, a third wave of the global financial crisis is now hitting the world's poorest and most vulnerable countries. The IMF and other donors must come to their aid. At its April summit, the G-20 committed significant resources to meet these needs:

- The G-20 agreed to a tripling of the resources available to the IMF to support its members to $750 billion. This increase in resources will be achieved by raising the number of participants in the IMF's "New Arrangements to Borrow" (NAB) from the current 26, enlarging the credit provided, and making the NAB more flexible, as well as by issuing notes to be acquired by member countries.[8] The IMF will use the money to buttress countries affected by the global downturn, including through the new precautionary credit lines. The expansion of the NAB is not a substitute for quota resources, however, and future quota increases will also expand the resources available to the Fund for providing financial support.

- The G-20 endorsed a doubling of the IMF's concessional lending capacity. As noted above, the IMF hopes to go further than this during the crisis years. Moreover, the G-20 signaled its willingness for the IMF to use part of the proceeds of a previously agreed sale of gold to support additional concessional financing for low-income countries, consistent with the IMF's new income model.

[8] An immediate doubling from $250 billion will come from bilateral pledges, including $100 billion each from Japan and the European Union, along with contributions from other bilateral creditors.

- The G-20 proposed that the IMF make a new general allocation of "special drawing rights," or SDRs, to inject $250 billion into the world economy and increase global liquidity. The injection would have a significant positive impact on developing countries, particularly low-income countries, as it would increase their international reserves and their ability to run counter-cyclical policies. The IMF's Executive Board is already discussing and proceeding with this mandate.

V. Strengthening the International Financial Architecture

There is now broad agreement on the contours of the crisis response and the critical importance of its coordination across countries. The challenge is to ensure that the steps taken now to resolve the immediate crisis also set the stage for more fundamental reforms of the global financial architecture that will strengthen financial systems and contribute to the prevention of future crises. The reforms undertaken should also address the problem of the fragmentation of surveillance and responsibility for different aspects of financial policy.

A. Financial Sector Regulation and Supervision[9]

The crisis offers useful lessons for financial sector regulation and supervision, the specifics of which are already being discussed in a number of fora, including the G-20, the Financial Stability Board, and the IMF. First, a macroprudential approach to supervision should be used and a clear mandate should be assigned for the oversight of systemic stability. Financial sector regulation and supervision should cover all possible sources of systemic risks, and should be activity-based, not institution-based, so as to encompass the relevant activities of currently unregulated or less regulated financial sector segments. Beyond the existing range of supervisory and regulatory powers aimed at controlling risks within individual financial institutions, measures are also needed to limit the risks that institutions pose to the overall system, to contain moral hazard, and to reduce procyclicality,[10] Such measures could reduce existing distortions and limit the incentives for excessive borrowing and lending. The levels of prudential oversight could be higher as the contribution of an institution to systemic risk increases. Systemic risk measures should also take account of the effects of leverage, funding, and interconnectedness among institutions.

Prudential regimes should incorporate incentives that support systemic stability and discourage regulatory arbitrage. Existing capital requirements should be adjusted to reduce their pro-cyclical effect—this could include requiring greater accumulation of capital in good times if credit is growing faster than GDP and the credit-to-GDP ratio is already high, with the extra capital serving as a buffer in downturns. Other prudential norms, including for liquidity, should also be adapted in a rules-based manner to help counter the cycle. More comprehensive information must be made available to regulators, central banks, and investors, with more detailed disclosure and reporting requirements, particularly for lightly regulated financial institutions and 'off-balance sheet' transactions, as well as over-the-

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[9] See *Lessons of the Financial Crisis for Future Regulation of Financial Institutions and Markets and for Liquidity Management*, IMF, February 2009 (http://www.imf.org/external/np/pp/eng/2009/020409.pdf).

[10] For example, capital and provisioning requirements and funding liquidity requirements should be re-examined.

counter derivatives markets. Steps to increase transparency should include increased disclosure of credit rating agency methodologies.

To be effective, national regulations and oversight provisions must be carefully coordinated internationally, to correctly assess systemic risks associated with cross-border transactions and institutions, enable joint remedial action across borders and appropriate burden sharing, where necessary, and to reduce the scope for regulatory arbitrage. Political and legal obstacles to effective regulation of cross-border institutions must be removed, and ground rules for collaboration on cross-border financial issues should be established. These could take the form of home-host agreements on risk assessment, applied through colleges of supervisors, and enhanced arrangements for supervision and resolution of cross-border financial institutions within harmonized or coordinated joint action frameworks.

An important role has been assigned to the IMF by the G-20 in the area of financial sector oversight and regulation. The IMF will continue its joint efforts with the Financial Stability Board (FSB), the World Bank, and the Basle Committee on Banking Supervision (BCBS) to develop an international framework for cross-border bank resolution arrangements; the IMF and the FSB will produce guidelines for national authorities to assess whether a financial institution, market, or instrument is systemically important, focusing on what institutions do rather than their legal form; and to strengthen adherence to international prudential, regulatory and supervisory standards, the IMF and the FSB, in cooperation with international standard-setters will provide an assessment of implementation by relevant jurisdictions, building on existing joint IMF/World Bank Financial Sector Assessment Programs (FSAPs), where they exist.

B. Surveillance[11]

The shortcomings of surveillance in identifying the mounting risks and motivating timely remedial action prior to the crisis underscore the need to expand the conduct and coverage of surveillance and increase its effectiveness and traction. Interlinkages were missed and the connections between macroeconomic risks and developments in domestic and international financial markets were underestimated—the risk arising from growing financial complexity and rising leverage, as well as the systemic risks resulting from links between financial markets, spillovers across national borders, and the strength of the resulting financial sector feedbacks onto the real economy.

Looking forward, further enhancements to the practice and coverage of surveillance are necessary to achieve a less fragmented and more pointed surveillance system that focuses on sources of systemic risk in advanced and emerging market economies (including from cross-border capital flows, credit bubbles and currency misalignments), and generates warnings and policy advice that are more likely to gain traction with policy makers. The new system should bring together the expertise and perspectives of a diverse range of institutions, and

[11] See *Initial Lessons of the Crisis for the Global Architecture and the IMF*, IMF, February 2009 (http://www.imf.org/external/np/pp/eng/2009/021809.pdf).

have a process to drill down on poorly-understood issues to improve risk assessments and related policy advice.

A key element of the system would be the joint work of the IMF and Financial Stability Board (FSB) on an early warning exercise (EWE), which has been intensified based on the lessons drawn from the analysis of the causes of the crisis. The EWE will integrate surveillance by combining the IMF's macro-financial expertise with the FSB's focus on financial systems. This exercise would identify evolving global concerns; organize them into a limited number of key underlying vulnerabilities, risks, and evolving trends; and provide pointed advice to policy makers on how to mitigate risks. Work on the EWE has already led to deeper analysis of financial markets and macro-financial linkages, the risks relevant to global or regional stability, and the systemic risks and appropriate treatment of non-bank financial institutions.

Another important part of efforts to enhance the effectiveness of surveillance is the joint work of the IMF and FSB to identify and work to close the data gaps revealed by the crisis. A wide range of users are being consulted and, with the results of this outreach, a program is to be developed to close these gaps, in consultation with other international agencies that disseminate economic and financial data. The need to better understand financial complexities and cross-border linkages, and to improve balance sheet data to monitor vulnerabilities, are emerging as clear themes from the initial discussions.

Equally importantly, the IMF's financial analysis will be better integrated with its macroeconomic work, through more risk-based and thematic assessments, with greater emphasis on external linkages and spillovers (including, possibly, through regional surveillance reports where appropriate).

C. IMF Governance and Global Economic Policy Coordination

Important progress was made in the reform of the IMF's governance in 2006-08, including the initiation of a process to realign members' voting power. However, enhancing the IMF's legitimacy and effectiveness must also deal with the question of whether the significant changes since the establishment of the Fund require reform of its institutional framework.The crisis response, and particularly the need to coordinate fiscal stimulus packages, has underscored the importance of global coordination of policies and measures. Given the integration of global markets, and the openness of capital markets, coordination of many aspects of fiscal and monetary policy is needed to enhance their effectiveness. More generally, collective action is needed to resolve some economic problems, most notably the unwinding of global imbalances and the prevention of their future accumulation. The IMF has the mandate, analytical expertise and institutional capacity to be the natural locus of this multilateral collaboration, but needs to overcome certain deficiencies that have generated dissatisfaction within the membership.

Quotas and voice

The membership adopted in April 2008 an important reform of the quota formula and an *ad hoc* increase of quotas designed to rebalance the IMF's quota shares to reflect better the evolving world economy, and further impetus given by the IMFC in April 2009.

The reforms adopted in April 2008, which still require legislative approval in member countries, aim at giving greater weight to the more dynamic emerging market economies and enhance the participation and voice of low-income countries in the IMF's decision making. In particular, through the aggregate impact of increases in quotas and a tripling of basic votes for all members, 135 countries will increase their voting share, with an aggregate shift in voting shares for these countries of 5.4 percentage points, including substantial increases for low-income countries.

This reform is all the more important given the IMF's expanded mandate in dealing with the crisis. In this context, the G-20 leaders committed to implementing the package of IMF quota and voice reforms agreed in April 2008 and agreed to bring forward the next general review of quotas with a view to its completion by January 2011.

The IMFC also emphasized on April 25 that "early action by national authorities to make the April 2008 agreements on quota and voice reform effective is crucial", indicated its expectation that the upcoming review of Fund quotas would result "in increases in the quota shares of dynamic economies, particularly in the share of emerging market and developing countries as a whole", and looked forward to "further work by the Executive Board on elements of the new quota formula that can be improved before the formula is used again". The IMF is proceeding rapidly with consideration of such reforms.

Broader issues of governance and the policy-making framework

In its April 2009 Communiqué, the IMFC indicated that "broader reforms to ensure the International Monetary and Financial Committee's active participation in the Fund's strategic decision making process should be promptly considered." The Executive Board will report back to the IMFC on enhancing the IMF governance structure by the next Annual Meeting in October 2009, taking into account input and proposals by various groups, both in the official community and civil society. Among the proposals that have been tabled for consideration are the formation of a high-level ministerial council to foster political engagement in strategic and critical decisions, a broader mandate for surveillance, clearer lines of responsibility and accountability between various decision-making entities in the Fund, and the introduction of an open and transparent selection process for the Managing Director, independent of nationality.

RELEVANT DOCUMENTS

Key Factors Behind the Crisis

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- IMF Resources and the G-20 Summit—Questions and Answers, April 2009 (http://www.imf.org/external/np/exr/faq/sdrfaqs.htm)
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- IMF Lending—Factsheet, March 2009 (http://www.imf.org/external/np/exr/facts/howlend.htm)
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- IMF Overhauls Nonconcessional Lending Facilities and Conditionality—Public Information Notice 09/40, April 2009
- Review of the Analytical Underpinnings of IMF Lending, Public Information Notice 09/41, April 2009
- IMF Reviews Access Limits, Charges and Maturities—Public Information Notice 09/42, April 2009 (http://www.imf.org/external/np/sec/pn/2009/pn0942.htm)
- IMF Implements Major Lending Policy Improvements—Background Note, March 2009 (http://www.imf.org/external/np/pdr/fac/2009/032409.htm)
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