INTERNATIONAL MONETARY FUND

Annual Report 2007

Making the global economy work for all

The International Monetary Fund

The IMF is the world's central organization for international monetary cooperation in which almost all countries in the world work together to promote the common good. The IMF's primary purpose is to safeguard the stability of the international monetary system—the system of exchange rates and international payments that enables countries (and their citizens) to buy goods and services from each other. This is essential for achieving sustainable economic growth and raising living standards.

All of the IMF's 185 member countries are represented on its Executive Board, which serves as a forum where they can discuss the national, regional, and global consequences of their economic policies. This *Annual Report* covers the activities of the Executive Board and Fund management and staff during the financial year May 1, 2006, through April 30, 2007.

The main activities of the IMF include

- providing advice to members on adopting policies that can help them prevent or resolve a financial crisis, achieve macroeconomic stability, accelerate economic growth, and alleviate poverty;
- making financing temporarily available to member countries to help them address balance of payments problems—that is, when they find themselves short of foreign exchange because their payments to other countries exceed their foreign exchange earnings; and
- offering technical assistance and training to countries at their request, to help them build the expertise and institutions they need to implement sound economic policies.

The IMF is headquartered in Washington, DC, and, reflecting its global reach and close ties with its members, also has offices in more than 80 countries around the world.

The IMF's financial statements for the year ended April 30, 2007, can be found on the CD-ROM affixed to the inside back cover of this *Report*. Additional information on the IMF and its member countries can be found on the Fund's Web site, *www.imf.org*.

Preface from the Executive Board

This *Annual Report* of the Executive Board of the IMF to the Board of Governors covers the financial year 2007, which began on May 1, 2006, and ended on April 30, 2007. Two events that occurred after the close of FY2007 are of such importance for the IMF, however, that they merit a mention in this preface.

The first is the Executive Board's decision in June 2007 to revise the Fund's framework for surveillance. In the three decades since the original framework was established by the Executive Board in 1977, the nature of the challenges faced by our members has changed. When the 1977 decision was adopted, the most serious threats to international financial and macroeconomic stability were the manipulation of exchange rates by countries seeking to correct their balance of payments problems, and short-term exchange rate volatility. Today, in our increasingly globalized world, as international trade and cross-border capital flows reach unprecedented levels, the most serious threats are fundamental exchange rate misalignments and capital account vulnerabilities. The new decision, which has broad support across the membership, reflects the current environment and provides our members with clear guidelines on the expectations of the international community regarding the potential spillover effects of exchange rate policies, and provides guidance to staff with a view to focusing the Fund's advice on macroeconomic policies that promote stability and growth.

The second event is Managing Director Rodrigo de Rato's announcement that he would step down in October 2007. On behalf of the Executive Board, I offer my gratitude to Mr. de Rato for his strong leadership and immense contributions to the Fund since he took up the reins in 2005. I would note, in particular, the Medium-Term Strategy launched in 2006, an ambitious program calling for reform of the distribution of quotas and voting power in the Fund to ensure that all members are fairly and adequately represented, and setting in motion important changes in Fund operations and policies that will enable us to better meet the evolving needs of our members. In the process of selecting Mr. de Rato's successor, Executive Directors have been invited to nominate candidates who have distinguished records as economic policymakers at senior levels and who are nationals of any of the Fund's 185 member countries. The Executive Board will consider these candidates in September.

Readers can find information about these and other developments after the close of the financial year at *www.imf.org,* the IMF's Web site.

The Executive Board is rightly proud of this new format of the IMF's *Annual Report.* To shape it into a more effective communication tool, the Executive Board decided to streamline the *Report* and to have it translated into seven languages—Arabic, Chinese, French, German, Japanese, Russian, and Spanish—three more than in the past. Readers will find all of the appendixes—including the financial statements—that used to be in the print *Report* on the CD-ROM affixed to the inside back cover. On the CD-ROM, they will also find Public Information Notices, press releases, assorted reports, and tables and boxes offering more detail on the activities described in the print *Report.*

We trust that readers will welcome these changes, and we invite your feedback.

Jonathan T. Fried
Chairman
Executive Board Committee on the Annual Report

Contents

Boxes

Tables

Figures

The IMF's financial year is May 1 through April 30.

The unit of account of the IMF is the Special Drawing Right (SDR); conversions of IMF financial data to U.S. dollars are approximate and provided for convenience. On April 30, 2007, the SDR/U.S. dollar exchange rate was US$1 = SDR 0.65609, and the U.S. dollar/SDR exchange rate was SDR 1 = US$1.52418. The year-earlier rates (April 30, 2006) were US$1 = SDR 0.67978 and SDR 1 = US$1.47106.

"Billion" means a thousand million; "trillion" means a thousand billion; minor discrepancies between constituent figures and totals are due to rounding.

As used in this *Annual Report,* the term "country" does not in all cases refer to a territorial entity that is a state as understood by international law and practice. As used here, the term also covers some territorial entities that are not states but for which statistical data are maintained on a separate and independent basis.

Message from the Managing Director

This is a time of transformation, in the global economy and in the International Monetary Fund. The sources of global growth have broadened: Europe, Japan, and the United States have all enjoyed solid economic performance over the past year, while middle-income emerging economies, including China and India, were also important contributors to global growth. Innovation in financial markets has continued, bringing with it many opportunities and some new risks. In the Fund, work on the reforms set out in the Medium-Term Strategy has proceeded, and we saw its first fruits in Financial Year 2007.

Some of the most important changes we have made in the past year have been in our economic oversight function, or surveillance, which is the Fund's core activity. The introduction of multilateral consultations gives the Fund—and the international community—an important new tool to forge consensus on approaches to common problems. The first multilateral consultation, which focused on reducing global imbalances while sustaining strong global growth, resulted in the five participants—China, the euro area, Japan, Saudi Arabia, and the United States—jointly setting out their policy plans in a document circulated at our Spring Meetings to ministers representing the Fund's 185 members. The participating countries putting forward these policies and discussing them collaboratively shows their commitment to multilateralism. As they are implemented, these policy plans will reduce global imbalances while helping to sustain growth.

The Fund also made important progress in deepening its work on financial markets and financial systems. We are better integrating our work on financial sectors with our work on macroeconomic issues. And through the merger of two Fund departments into the Monetary and Capital Markets Department in June 2006, we have established a center of excellence in financial market issues—an area of growing importance to the global economy and to the Fund's members.

In FY2007 we also began work on reforms of the legal framework for bilateral surveillance, which culminated in an Executive Board Decision on a New Framework for Surveillance early in FY2008. The new decision is the first major revision of the surveillance framework in some 30 years, and has broad support from our membership. It reflects current best practice in our work of monitoring members' exchange rate policies and domestic economic policies; reaffirms that surveillance should be focused on the Fund's core mandate—promoting countries' external stability; updates the principles for the guidance of members in the conduct of their exchange rate policies; and sets out clearly what is expected of surveillance, including candor and evenhandedness.

The Fund's work with low-income countries has remained intense. Ten new programs under the Poverty Reduction and Growth Facility were approved last year, and 24 countries have now benefited from debt relief under the Multilateral Debt Relief Initiative. We are also taking steps to ensure that we are focusing on critical macroeconomic and financial areas, which is where we can make the greatest contribution to stability, growth, and poverty reduction in low-income countries. We will continue to work in partnership with the World Bank and other development agencies, and in doing so can now draw on an important report on Bank-Fund collaboration by a committee of external experts headed by Pedro Malan. The Committee's report, delivered in February 2007, will help us clarify roles and work better with our World Bank colleagues.

Technical assistance and training remain important elements of our work, especially in low-income countries. FY2007 saw the opening of a regional technical assistance center in Libreville, Gabon, the third in Africa, as well as the opening

Rodrigo de Rato, IMF Managing Director and Chair of the Executive Board

of the Joint Indian-IMF Training Program in Pune, India, the seventh regional training center worldwide. Meanwhile, the consolidation of anti–money laundering and combating the financing of terrorism (AML/CFT) activities in the Fund's Legal Department has made it the largest multilateral provider of technical assistance on AML/CFT.

In January 2007, we received a report from a Committee of Eminent Persons chaired by Andrew Crockett. Arguing that the Fund needs a new income model and that it should not continue to rely almost entirely on lending to finance public goods such as surveillance and technical assistance, the Crockett Report recommended that the Fund broaden its sources of income. Establishing reliable income sources—together with effective management of expenditure—is important to give our members confidence that the Fund will be able to carry out its mandate in the future and to enable us to make reliable plans to implement agreed policies. We have already acted on expenditure: the medium-term budget for FY2008–10 implies a reduction in the IMF's real administrative resources in each of the next three years, to be achieved by increasing efficiency and by scaling back or eliminating lower-priority activities. Addressing the income side of the equation will be a major priority for FY2008.

The September 2006 Annual Meetings were held in Singapore. The meetings gave all of our members a chance to see how far Asia has come since the crisis a decade ago. They also saw the Fund take a major step forward with the completion of the first stage of reform of quotas and voice. On September 18, 2006, our Board of Governors approved ad hoc quota increases for four countries—China, Korea, Mexico, and Turkey—that were clearly underrepresented and agreed on more fundamental reforms to be delivered within two years. This was a historic agreement for the Fund. In January 2007, the Executive Board began work on a proposed amendment to the Articles of Agreement to increase basic votes, with the aim of protecting the voting share of low-income countries as a group. And at its meeting on April 14, 2007, the International Monetary and Financial Committee (IMFC) gave us guidance on a new formula for broader changes in quotas. The IMFC agreed that the new formula should be simple and transparent, and appropriately capture the relative positions of members in the global economy. The reform should also result in higher shares for dynamic economies, many of which are emerging market economies, whose weight and role in the global economy have increased. Our objective remains to complete these reforms by the 2007 Annual Meetings if possible, and by no later than the 2008 Annual Meetings. Meeting this target will require leadership from members, and compromises among them. But if we can continue to draw on the spirit of multilateral cooperation that we saw in Singapore then I am confident that we will succeed.

The past year has been a year of great change at the Fund, and there are many changes still to come. There have also been changes in staff and management. Anne Krueger, First Deputy Managing Director from 2001 to 2006, has been succeeded by John Lipsky. Agustín Carstens, Deputy Managing Director from 2003 to 2006, has become Secretary of Finance of Mexico and has been succeeded by Murilo Portugal. Among the changes to come will be my own departure. I will step down as Managing Director after the 2007 Annual Meetings.

However, there are also important continuities: in the commitment to the Fund of our members, represented by our excellent Executive Board; in the dedicated career staff of the Fund; in the work of the institution; and in our sense of vision and purpose. I am proud to be have been able to help guide the Fund during this time of change, and to have had the opportunity to serve all of the members of this great institution.

The IMF Executive Board and senior management

Letter of Transmittal to the Board of Governors

August 3, 2007

Dear Mr. Chairman:

I have the honor to present to the Board of Governors the Annual Report of the Executive Board for the financial year ended April 30, 2007, in accordance with Article XII, Section 7*(a)* of the Articles of Agreement of the International Monetary Fund and Section 10 of the IMF's By-Laws. In accordance with Section 20 of the By-Laws, the administrative and capital budgets of the IMF approved by the Executive Board for the financial year ending April 30, 2008, are presented in Chapter 5. The audited financial statements for the year ended April 30, 2007, of the General Department, the SDR Department, and the accounts administered by the IMF, together with reports of the external audit firm thereon, are presented in Appendix VI. The external audit and financial reporting processes were overseen by the External Audit Committee, comprising Dr. Len Konar (Chair), Mr. Satoshi Itoh, and Mr. Steve Anderson, as required under Section 20*(c)* of the Fund's By-Laws.

Rodrigo de Rato
Managing Director and Chair of the Executive Board

Chapter 1

Chapter 1 Overview

During the financial year beginning on May 1, 2006, and ending on April 30, 2007, the Executive Board focused on adapting Fund policies and operations to better meet the evolving needs of the IMF's member countries, whose number increased to 185 in January 2007, when Montenegro joined. Although many of the IMF's members experienced another year of strong economic growth and favorable market conditions, the economic and financial environment was not without risk. Large global imbalances persisted, the U.S. economy slowed, prices for oil and nonfuel commodities remained high, and investors continued to show a large appetite for risky assets.

The IMF made considerable progress in implementing the objectives set out in the Medium-Term Strategy (MTS) launched by the Managing Director in FY2006 (Box 1.1). With capital flows to emerging market economies reaching unprecedented levels in recent years, and demand for Fund lending declining as a result, the IMF has been increasingly concentrating on surveillance,[1] policy advice, and technical assistance. During FY2007, it developed a new surveillance vehicle—the multilateral consultation—with which it sought to help its members address the problem of global imbalances. It also began a review of its framework for surveillance and moved to better integrate financial sector work into its surveillance activities to help members manage the risks associated with, and reap the benefits from, globalized financial markets.

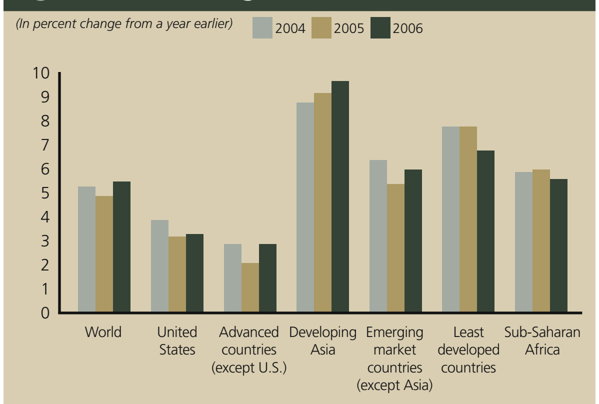
In recognition of the growing economic weight of some Fund members, the Executive Board undertook quota and governance-related reforms designed to ensure the fair distribution of quotas and adequate representation of all members. The Board also took steps to improve the Fund's internal governance, enhance the efficiency of Fund operations, and develop a new income model more closely aligned with the variety of functions the institution now performs.

1 The monitoring of global, regional, and national economic policies; see Box 2.1.

Key Economic and Financial Developments

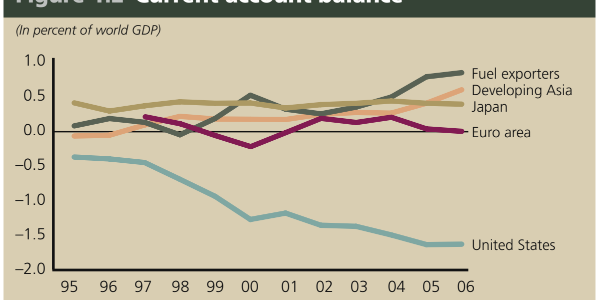
Global economic growth accelerated to 5.4 percent in 2006—up from 4.9 percent in 2005—marking the fourth successive year of a strong global expansion (Figure 1.1). Moreover, the expansion became better balanced, as a slowing in the U.S. economy was offset by firming of growth elsewhere. Emerging market countries grew particularly fast, supported by benign international financial conditions and, in many cases, high commodity prices. Inflation in the advanced economies declined in the second half of 2006 as oil prices fell from a peak in August.

Figure 1.1 Real GDP growth



Current account imbalances continued to be large (Figure 1.2). The external deficit of the United States stabilized at 6½ percent of GDP in 2006, with a marked narrowing toward the end of the year. The surpluses of the oil-exporting and East Asian countries continued to rise, while deficits grew in both western and emerging Europe[2] and in rapidly growing emerging market economies such as India.

Figure 1.2 Current account balance



Growth in the *United States* slowed markedly, declining from an annual rate of 2½ percent in the second half of 2006 to 0.6 percent in the first quarter of 2007, primarily because of declines in net exports, inventories, and residential investment. Although export growth remained solid, faster import growth reversed some of the improvement that had been made in the trade balance after August 2006. Rising oil imports accounted for more than half of the increase in imports. Business investment also slowed. However, private consumption remained solid, supported by continued employment growth and rising equity prices.

Economic activity in the *euro area* gained momentum during the same period. GDP growth reached 2½ percent (seasonally adjusted annual rate) in the first quarter of 2007, almost double the pace in 2005 and the highest rate since 2000, driven by strong investment and net exports, while consumption spending slowed significantly, reflecting in part the impact of the increase in the German value-added tax.

Japan's economic expansion hit a soft patch in the middle of 2006, mainly because of an unexpected decline in consumption, but growth rebounded strongly in the fourth quarter of 2006 as domestic demand regained momentum. The pace of activity moderated in early 2007, but growth remained above potential.

Activity in *emerging Asia* continued to expand briskly, led by strong growth in China and India. In China, real GDP grew by 10.7 percent in 2006. The pace of fixed-asset investment cooled in the second half of 2006 but gathered pace again in early 2007. India's growth of 9.7 percent in 2006 was supported by strong consumption and, especially, investment. In the newly industrialized economies (Korea, Taiwan Province of China, Hong Kong SAR, and Singapore), resilient external demand supported activity, notably in the electronics sector. GDP growth also increased in the ASEAN-4 economies (Indonesia, Malaysia, the Philippines, and Thailand).

Growth in *Latin America* accelerated to 5.5 percent in 2006 from 4.6 percent in 2005, bringing the average growth rate for the past three years to 5¼ percent, the best performance since the late 1970s. Growth picked up in Brazil and Mexico, although it remained below the regional average. As Latin America's recovery matured, domestic demand became the main engine of growth. Net exports exerted a downward pull

2 *As used in Fund publications, this term includes Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Romania, the Slovak Republic, and Turkey.*

Box 1.1 Progress on implementing the Medium-Term Strategy

	Objective	Action
Surveillance	Modernizing the framework	Review of 1977 Decision on Surveillance over Exchange Rate Policies and work on a "remit" (statement of surveillance priorities)
	Taking a multilateral perspective and strengthening financial sector surveillance	First multilateral consultation; expansion of regional surveillance; greater analysis of cross-country spillovers; increased financial sector coverage; report of task force on integrating financial sector work into surveillance
	Making country surveillance sharper and more focused	Surveillance agendas; experimentation with streamlined consultations
Emerging markets and crisis prevention	Deepening financial sector and capital market surveillance	Development of a framework for addressing financial sector issues in country surveillance
	Reassessing the adequacy of existing instruments for crisis prevention	Board discussions and outreach on the development of a new contingent financing instrument for liquidity problems as part of the IMF's crisis-prevention toolkit
Low-income countries	Supporting the international community's effort to help low-income countries achieve the Millennium Development Goals	Policy advice, concessional lending, debt relief, and technical assistance to help low-income countries achieve macroeconomic stability and accelerate growth; tracking progress toward Millennium Development Goals jointly with the World Bank *(Global Monitoring Report)*
	Deepening involvement in dealing with aid flows	Policy advice on the effective use of increased aid; following up on the recommendations of the Independent Evaluation Office's report on the IMF's advice and actions with respect to aid flows to sub-Saharan Africa
	Helping countries that have received debt relief avoid reaccumulating unsustainable debt	Improvements in the Debt Sustainability Framework and greater outreach; technical assistance on improving public debt management practices and enhancing statistical capacity
Capacity building	Bolstering capacity building in developing countries; better integrating technical assistance and training with surveillance in accordance with country priorities	Implementing the MTS for capacity building; integrating country needs and technical assistance resources with the IMF's budget process; working closely with donor partners to leverage internal resources for capacity building; expanding regional technical assistance and training activities, including with the opening of the third regional technical assistance center in Africa (the sixth worldwide), and a new regional training center in India (the seventh worldwide)
Quota and voice reform	Reinforcing IMF effectiveness and legitimacy through progress on quota and voice reform	Ad hoc quota increases for four clearly underrepresented countries—China, Korea, Mexico, and Turkey; consideration of principles for new quota formula; discussion of the legal framework for increasing basic votes; increasing staff resources for Executive Directors elected by a large number of members
Governance and management	Strengthening communication and transparency	Beginning of review of communication strategy; release of second transparency annual report
	Making the IMF more cost-effective and efficient	Consideration of recommendations of external committee report on Bank-Fund collaboration; implementation of output-oriented budget framework with real reduction in resources over the medium term; improved risk-management framework; streamlining procedures
	Putting the IMF's finances on a sustainable footing	Report on the IMF's income model by Committee of Eminent Persons

on activity, partly as a consequence of weaker growth in the United States, the region's largest trading partner, although commodity exporters continued to benefit from buoyant world commodity prices.

In ***emerging Europe,*** growth accelerated to 6 percent in 2006. Domestic demand increased as consumption was boosted by rising employment and real wages. Current account deficits widened further but, in most cases, were financed without difficulty by bank inflows and foreign direct investment. However, concerns about large external deficits in Hungary and Turkey led to downward pressure on the exchange rates for those two countries, and policies were tightened. Activity in the ***Commonwealth of Independent States,*** the group formed by 12 of the former Soviet republics, also continued to expand briskly, supported by high prices for oil and non-oil commodities.

Middle Eastern oil exporters enjoyed another year of solid growth in 2006, accompanied by strong external and fiscal balances. Oil revenues continued to grow rapidly, the strong momentum of the non-oil sector continued, and governments planned large expenditures on social programs and investment in the oil and non-oil sectors.

Growth in ***sub-Saharan Africa*** moderated somewhat in 2006 but remained robust, driven increasingly by domestic investment, rising productivity, and, to a lesser degree, government consumption. Higher oil revenues and debt relief supported government spending in many countries. Inflation remained subdued for most, owing to prudent macroeconomic policies and another good harvest.

Oil prices continued to be high and volatile. After reaching a record high of $76 a barrel in August 2006, the average petroleum spot price declined in subsequent months, reflecting a combination of slowing demand in industrial countries, a recovery of non-OPEC supply, and some easing of geopolitical tensions. However, OPEC's production cuts after November and a recovery in demand in the first quarter of 2007 caused prices to rebound. Renewed geopolitical tensions in the Middle East pushed prices up even further in March and April of 2007, to $65 a barrel by the end of April. Prices of ***nonfuel commodities,*** led by metals, also rose sharply during the second half of 2006 and the first four months of 2007, as did prices of some agricultural commodities—notably corn—reflecting, in part, the prospect of growing demand for biofuels.

Container terminal, Hamburg, Germany

The ***monetary policies*** adopted by IMF member countries reflected different cyclical positions. The U.S. Federal Reserve kept the Fed funds rate on hold from June 2006 on, balancing the risks of a cooling economy against continued concerns about inflation. With inflation in Japan continuing to hover around zero, the Bank of Japan raised its policy rate to 0.5 percent in two quarter-point moves, after abandoning its zero interest rate policy in July 2006. By contrast, the European Central Bank and European national central banks steadily tightened monetary policy. Some emerging market countries—notably China, India, and Turkey—also tightened monetary conditions, China and Turkey because of concerns about overly rapid growth, India because of concerns about inflationary pressures. Turkey was also responding to external pressures. Regarding ***fiscal policies,*** industrial countries made some progress in reducing structural deficits, largely as a result of unusually strong revenue growth. Nonetheless, with their aging populations, these countries will need to make further substantial adjustments going forward to achieve fiscal sustainability.

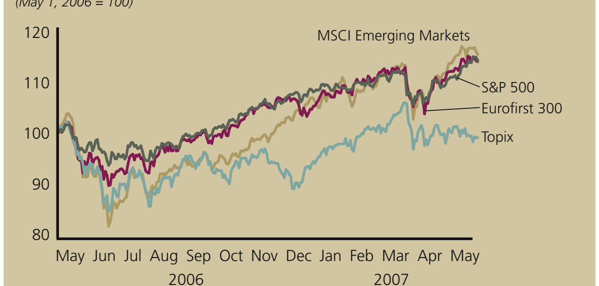
In ***foreign exchange markets,*** slower growth in the United States contributed to a weakening of the U.S. dollar. Between May 2006 and the end of April 2007, the dollar depreciated 8.4 percent against the euro and 9.5 percent against the British pound. The yen also weakened further, as low interest rates continued to encourage capital outflows. The renminbi depreciated slightly in real effective terms, despite a mild acceleration in its rate of nominal appreciation against the U.S. dollar and a further rise in China's current account surplus to 9½ percent of GDP in 2006. Overall, currency market conditions remained orderly and volatility, low.

Financial market stability continued to be underpinned by favorable global economic prospects. Despite bouts of nervousness in May/June 2006 and again in February/March 2007, market volatility generally remained at low levels. The latter episode was triggered by a variety of factors against a backdrop of growing concern about the impact of the rapidly slowing U.S. housing market on housing-related securities, as mortgage delinquencies and default rates picked up, particularly in loans to lower-quality (subprime) borrowers.

Corporate bond spreads remained low. Strong corporate balance sheets, including ample cash cushions, supported a wave of mergers and acquisitions. This activity, combined with higher-than-expected corporate profits, contributed to double-digit returns in most ***global equity markets,*** Japan being a notable exception (Figure 1.3). During the IMF's financial year 2007, the S&P 500 gained 13.1 percent and the Eurofirst 300 gained 13.9 percent, while the Topix lost 0.9 percent.

Figure 1.3 Equity market performance

(May 1, 2006 = 100)

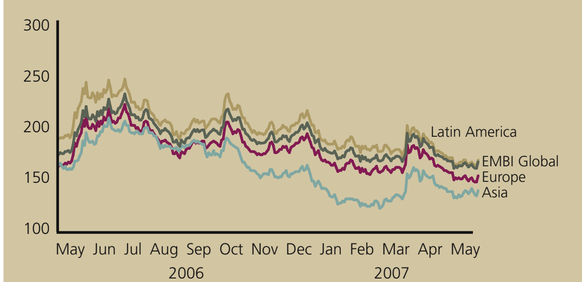


Source: Bloomberg L.P.

In emerging markets,[3] yield spreads declined to new historical lows (Figure 1.4). The market was supported by continued improvements in credit quality (with rating upgrades far exceeding downgrades), more sovereign debt buybacks (and, in the process, the continued reduction of the stock of Brady bonds), and reduced sovereign issuance. Global investors increased their portfolio allocations in local emerging markets. Net flows to emerging equity markets fluctuated. In particular, sharp outflows were recorded during the corrections of May/June 2006 and February/March 2007, with the largest outflows experienced in those markets that had run up the most. Nonetheless, emerging market equities produced strong returns, with the MSCI local currency emerging market equity index gaining 15.2 percent between May 1, 2006, and end-April 2007.

Figure 1.4 Sovereign spreads

(In basis points)



Source: JPMorgan Chase & Co.

Highlights of the Work of the Executive Board

The common thread running through the IMF's activities in FY2007 was the continued acceleration of globalization, the greatest challenge facing both the IMF and its members in the early twenty-first century. With this challenge in mind, the Executive Board made considerable progress toward key objectives set forth in the Fund's MTS: strengthening and modernizing surveillance; seeking new ways to support emerging market countries; deepening Fund engagement with low-income countries; reforming governance and strengthening internal management to make the Fund a more efficient and effective institution; and placing the IMF's finances on a sustainable footing.[4]

3 *Emerging market economies are mainly developing countries that have advanced far enough in capital market development to attract foreign portfolio investment and/or borrow significantly in international capital markets.*

4 *The Executive Board's calendar and work program can be found on the CD-ROM. General information on the Board's responsibilities and activities can be found in the* IMF Handbook, *also on the CD-ROM.*

Strengthening and modernizing surveillance

To serve the purposes of the IMF's membership, surveillance must be focused, candid, transparent, evenhanded, and accountable, and devote careful attention to cross-country spillovers. In FY2007, the Executive Board took steps to strengthen and modernize the framework for surveillance. It began a review of the 1977 Decision on Surveillance over Exchange Rate Policies, the framework adopted by the Board in 1977 that has guided the IMF's work in this area, to ensure that it reflects best practice and sets out a coherent vision of the IMF's core activity. In their review, Executive Directors found important areas of broad agreement, and, during the period covered by this *Report,* worked to build common ground in other areas. They also examined possible ways to introduce more explicit priorities for surveillance and more rigor in the IMF's methodologies for assessing the effectiveness of its surveillance work.

The Board supported several innovations in the implementation of surveillance. Among these was the IMF's first multilateral consultation, which focused on fostering common understanding and cooperation on how to reduce global imbalances while sustaining strong global growth. In addition, the framework for surveillance of the financial sector and capital markets was strengthened, based in part on the recommendations of an internal task force on integrating the financial sector into the surveillance work of the IMF. The task force urged the IMF to make better use of the Financial Sector Assessment Program (a joint IMF–World Bank initiative described in detail in Chapter 2) in the context of country surveillance and to devote more attention to the links between the financial sector and the macroeconomy. As called for in the MTS, the IMF's analytical tools were increasingly applied to capturing cross-country spillovers and drawing policy lessons, while regional surveillance continued to be expanded, with a view to deepening understanding of the impact of regional developments on both the global economy and national economies. The Board advocated sharpening country surveillance, calling on staff to focus on the most important risks confronting members and on topics that are core to the IMF's mandate. The IMF also experimented with streamlined Article IV consultations for a small number of countries.

The IMF's first multilateral consultation focused on reducing global imbalances while sustaining strong global growth. China, the euro area, Japan, Saudi Arabia, and the United States participated.

High oil prices complicated policymaking, and the Board provided advice to both exporters and importers of oil on appropriate policy responses, bearing in mind that rising demand, production constraints, and supply disruptions could pose a threat to global growth or fuel inflationary pressures. The Board continued to emphasize the need for more investment in the oil sector and encouraged member countries to pass international oil prices through to consumers in order to avoid a distortion of consumption patterns.

The Board's discussions of the *World Economic Outlook* and the *Global Financial Stability Report,* the IMF's primary vehicles for global surveillance, and other issues related to the IMF's surveillance activities in FY2007 are described in greater detail in Chapter 2.

Program support

Many ***emerging market economies*** have strengthened their policies, addressed vulnerabilities, and improved debt structures. Some—particularly in Asia—have accumulated large reserves and expanded regional reserve pooling arrangements. The prospects for emerging market economies remain positive, with favorable financial conditions and further robust growth expected to continue. As a result, most are now able to meet their financing needs for the coming year in the international financial markets, and their demand for IMF lending has declined dramatically. Nonetheless, macroeconomic fundamentals still vary widely among emerging market economies and vulnerabilities remain.

In FY2007, the Executive Board considered ways to strengthen the IMF's support for emerging market economies. Given their growing reliance on international capital flows, the deepening of financial sector and capital market surveillance would have particular relevance for these economies' crisis-prevention efforts. The Board also made progress toward developing an instrument that would make financing available to emerging market economies with sound policies in the event of a temporary loss of liquidity. Recognizing that a member's own policies are central to crisis prevention, the Board considered a staff paper on the sources and costs of shocks and the policy options that can best insulate members from crisis.

Over the past few years, the IMF has broadened the array of financing and other instruments available to low-income countries.

The Executive Board also explored ways to deepen the IMF's engagement with ***low-income countries,*** in collaboration with the World Bank, while focusing on helping them achieve macroeconomic stability and accelerate growth, the areas in which the IMF is best equipped to assist as they strive to reduce poverty and achieve the Millennium Development Goals.

Over the past few years, the IMF has broadened the array of financing and other instruments available to low-income countries. In FY2007 the Executive Board focused on finding ways to help countries that have received debt relief—through the Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI)—avoid building up new unsustainable debt burdens. The Board provided advice on putting in place the kinds of macroeconomic policies that will allow low-income countries to use aid effectively, and reviewed a report by the Independent Evaluation Office (IEO; see Box 5.3) on the IMF's prior advice and actions with respect to aid flows to sub-Saharan Africa (the IEO's findings are discussed in Chapter 3). Given that the economic development of low-income countries depends crucially on trade, the Executive Board urged Fund members to work toward a successful conclusion to the Doha Round of multilateral trade negotiations. The IMF also continued to offer technical assistance in such areas as tax and customs reform to enable low-income countries to benefit fully from trade liberalization, and stood ready to provide financial assistance to countries that might be harmed in the short run by other countries' trade liberalization.

A table detailing the instruments through which the IMF provides financial and other assistance to member countries can be found in Chapter 3 (Table 3.1), along with more information about the IMF's lending activities and other program support in FY2007.

Capacity building

As country surveillance has become more focused, the close relationship between surveillance and capacity building has become increasingly apparent. The technical assistance and training provided by the IMF can help member countries implement the policy advice they receive during the course of surveillance. Work during FY2007 continued to focus on ensuring that technical assistance and training were more closely aligned with the priorities of both the IMF and recipient countries, and better coordinated with services provided by others.

In view of the critical need for additional capacity building in developing countries, the Central Africa Regional Technical Assistance Center (AFRITAC) was opened in Gabon to serve countries in that area and a new regional training program was established in India. The new AFRITAC—the third in Africa and the sixth regional technical assistance center worldwide—will complement the activities of the East AFRITAC and the West AFRITAC. The training center in India is the seventh such center worldwide, with other regional training centers located in Africa, East Asia, Europe, Latin America, and the

Middle East. The IMF began to develop a plan, in collaboration with the World Bank, to enhance capacity building in the design of medium-term debt strategies in both emerging market economies and low-income countries, to help them avoid the reaccumulation of unsustainable debt.

The process for allocating technical assistance resources has been improved with the introduction of medium-term regional plans that will be integrated with the IMF's budget process. The Board has also begun to explore ways to ensure adequate financing for capacity building amid growing demand, including by increasing external financing.

Quota and voice reform

If the IMF is to reinforce its legitimacy, it must truly represent—and must be seen as truly representing—all of its member countries. Thus, in FY2007, the Executive Board embarked on far-reaching quota and voice reforms, a central goal of the MTS, to better align members' quotas with their economic weight in the global economy and to enhance the participation and voice of low-income members.

In its communiqué of April 22, 2006, the International Monetary and Financial Committee (IMFC) emphasized the importance of governance reform to safeguard and enhance the IMF's effectiveness and credibility as a cooperative institution, and called for concrete proposals from the IMF's Executive Board by the time of the September 2006 Annual Meetings. In response to the Executive Board's recommendations,[5] on September 18, 2006, the Board of Governors adopted a Resolution on Quota and Voice Reform granting ad hoc quota increases for China, Korea, Mexico, and Turkey, the four most clearly underrepresented countries, and setting out a package of more fundamental reforms to be completed, if possible, by the Annual Meetings of 2007 and no later than the Annual Meetings of 2008.[6]

A work program involving consultations with the membership and informal and formal Board discussions on various elements of the package was initiated after agreement was reached on the Resolution. In a preliminary discussion in January 2007, the Board generally endorsed the overall framework proposed by Fund staff for an amendment to the

Girl on bus, Tanzania

IMF's Articles of Agreement related to an increase in basic votes.[7] It also considered additional staffing for Executive Directors representing large constituencies—namely, the two chairs for sub-Saharan Africa (see Chapter 5, footnote 58). In addition, the Board held two informal discussions on principles for a new quota formula that will form the basis for a second round of ad hoc increases. In its April 14, 2007, communiqué, the IMFC welcomed the progress to date and called on the Executive Board to continue its work on the reform package as a matter of priority.

Communication and transparency

The MTS stresses the importance of communication and transparency in enhancing the effectiveness of surveillance and in building support for sound economic policies. The Executive

5 *See Press Release 06/189, "IMF Executive Board Recommends Quota and Related Governance Reforms," on the CD-ROM or at* www.imf.org/external/np/sec/pr/2006/pr06189.htm.

6 *See Press Release 06/205, "IMF Board of Governors Approves Quota and Related Governance Reforms," on the CD-ROM or at* www.imf.org/external/np/sec/pr/2006/pr06205.htm, *as well as the Board's Resolution, which can be found on the CD-ROM.*

7 *As stipulated in the Articles of Agreement, each member country's voting power in the IMF is the sum of its 250 basic votes (the same for each member) and one vote per SDR 100,000 of its quota in the IMF. Until the mid-1970s, each member's basic votes accounted for more than 10 percent of total votes; however, general increases in quotas have since reduced that share to about 2 percent.*

Board plays a key role in the Fund's communication efforts, providing strategic guidance, conducting regular reviews of the IMF's communication strategy (the fifth review began during FY2007), and, more generally, approving the IMF's budget, which includes the resources allotted to communication and outreach. During FY2007, the Board identified concrete steps for strengthening the links between the IMF's operations and its communications, and for increasing the impact of communication and outreach—for example, by making key IMF documents more readily available in languages other than English, as described in greater detail in Chapter 5. The Executive Board's Committee on the *Annual Report* took steps to make the *Report* a more effective communication vehicle, not only for the IMF's official stakeholders but also for a broader audience.[8]

Executive Directors led the Fund's efforts to increase its transparency. In FY2006, they called on the staff to publish annual updates on the implementation of the Fund's transparency policy. The second annual update, released in February 2007, shows that the number of member countries choosing to publish—publication is voluntary—all reports on their economies and use of Fund resources increased to 142 in 2006, from 136 in 2005, and the percentage of such reports that were published increased for the third consecutive year.

Improving internal governance

The IMF is committed to becoming a more cost-effective institution, without compromising its ability to deliver the key outputs called for in the MTS. Hence a collective effort by the whole institution—the Board, the management, and the staff—is in train to enhance efficiency.

As discussed in more detail in Chapter 5, during FY2007, the IMF continued to strictly limit administrative expenditures. The medium-term budget called for zero growth, in real terms, in FY2007, and real reductions in FY2008 and FY2009. A number of initiatives were undertaken to deliver the IMF's outputs more efficiently and at a lower cost, including increased outsourcing, offshoring of some support services, and a reexamination of travel expenditures.

The IMF took steps during the year to strengthen its risk-management framework. The Executive Board regularly reviews the IMF's risk-management policies, and, in 2006, it adopted measures to implement a comprehensive risk-assessment system based on the recommendations of a task force. These measures focus on four broad categories of risks—strategic, core mission, financial, and operational. In FY2007, the IMF conducted its first risk-assessment exercise, which identified the main risks facing the IMF and the measures in place to mitigate them. In their discussion, Executive Directors stressed their oversight role and critical fiduciary responsibility for the IMF's risk management.

The Executive Board also acted to streamline Fund procedures, lengthening the intervals between most policy reviews, consolidating some reports, and eliminating others. It considered a report on Bank-Fund collaboration, which was prepared by an external review committee commissioned by IMF and World Bank management, and sought possible improvements in the way the two institutions work together that would enable the IMF to deliver policy advice and capacity-building services to member countries more effectively and efficiently (see Chapter 5). In addition, the Board reviewed the report by the Independent Evaluation Office (IEO) on the IMF and aid to sub-Saharan Africa and endorsed a number of recommendations that in its view would enable the IMF to improve its policies and operations in this region (Chapter 3).

Reviewing the finances of the Fund

In May 2006, the Managing Director appointed a Committee of Eminent Persons to study the IMF's income model. The Committee's report, submitted to the Executive Board and issued in January 2007, concluded that the IMF's current income model, under which the main source of income is the interest charged on loans, is not appropriate given the wide range of the IMF's functions and responsibilities.[9] The committee recommended a new set of revenue measures, including expanded investment guidelines and operations, the creation of an endowment from limited IMF gold sales, and charges for services to member countries. In its April 2007 meeting, the IMFC indicated that the committee's report provided "a sound basis for further work on the development of a new income model." The Board's work on a model that can garner broad support across the IMF's membership is ongoing.

8 *Although the print version of the current* Annual Report *is much shorter than past* Reports*, the* Report *remains a comprehensive document of record because much of the material previously included in the print version has been transferred to the CD-ROM accompanying the* Report.

9 *The report can be found on the CD-ROM or on the IMF's Web site, at* www.imf.org/external/np/oth/2007/013107.pdf.

Chapter 2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Chapter 2 Promoting financial and macroeconomic stability and growth through surveillance

The IMF monitors the international monetary and financial system to ensure that it is functioning smoothly and to identify vulnerabilities that could undermine its stability. To the same end, it oversees economic policies in its 185 member countries, offering members analysis and advice and encouraging them to adopt policies that promote financial and macroeconomic stability and sustained growth. The IMF's surveillance activities at the global and country levels are complemented by periodic assessments of regional developments, including the economic policies pursued under formal regional arrangements such as monetary unions. This combination of oversight and advice is known as surveillance (Box 2.1).

During FY2007, the IMF introduced several innovations in its surveillance work. It experimented with a new forum—multilateral consultations—where countries, or entities composed of groups of countries, can work together on common issues. The first multilateral consultation was set up by the IMF to help its members address the risks posed by current global imbalances. The IMF also devoted more attention to cross-country spillovers; increased its emphasis on regional developments in an effort to achieve a better understanding of how these affect individual countries as well as the global economy; sharpened the focus of its Article IV consultations, placing a greater emphasis on exchange rate and financial sector issues; and strengthened its outreach efforts, to promote good policies and build consensus around them (see Chapter 5 for more information on IMF outreach).

Going beyond changes in the day-to-day implementation of surveillance, the Executive Board worked to strengthen and modernize the IMF's surveillance framework. The Medium-Term Strategy (MTS) calls for more emphasis on the original goal of IMF surveillance—assessing the consistency of exchange rate and macroeconomic policies with national and international stability. In FY2007, the Executive Board reviewed the IMF's 1977 Decision on Surveillance over Exchange Rate Policies, which—together with Article IV of the Articles of Agreement—is the main statement guiding surveillance, and considered ways to clarify surveillance priorities.

The IMF also took steps to better integrate financial sector analysis into Article IV consultations and regional surveillance and to identify links between the financial sector and the macroeconomy. Supporting these efforts is the new Monetary and Capital Markets Department (MCM), which was created in early FY2007 (Box 2.2). As part of the reorganization of the IMF's financial sector work in FY2007, responsibility for work on issues related to anti–money laundering/combating the financing of terrorism (AML/CFT) was centralized in the IMF's Legal Department, which shares responsibility with MCM for policy and operational questions regarding the integration of AML/CFT into financial sector work.

Box 2.1 Surveillance activities

The IMF's Executive Board conducts surveillance at the global, country, and regional levels. Global surveillance is carried out through the Board's reviews of world economic and financial market developments and prospects. The staff's *World Economic Outlook* (WEO) and *Global Financial Stability Report* (GFSR), which are usually prepared twice a year, provide major inputs to the Board's discussions and are subsequently published. The Board also holds informal discussions of world economic and financial market developments. Another important instrument of global surveillance is the *Annual Report on Exchange Arrangements and Exchange Restrictions* (AREAER), which the Fund has published since 1950.[1]

When a country joins the IMF, it makes a commitment under Article IV of the IMF's Articles of Agreement to seek to pursue policies conducive to orderly economic growth and price stability and to avoid manipulating exchange rates for unfair competitive advantage. It also commits to providing the IMF with data about its economy. The IMF is mandated by Article IV to conduct surveillance to oversee members' compliance with these obligations, and it does so through regular (usually yearly) staff visits—known as Article IV consultations—to member countries.[2] (Informal staff visits often take place between consultations.) The IMF staff team collects economic and financial data and discusses with government and central bank officials economic developments since the previous consultation, as well as the country's exchange rate and monetary, fiscal, financial sector, and structural policies. Often, the team also meets with other groups such as legislators, trade unions, academics, and financial market participants. It prepares a summary of its findings and policy advice, which it leaves with the national authorities, who have the option of publishing it. On return to IMF headquarters, the staff team prepares a report describing the economic situation and the talks with the authorities and evaluating the country's policies. The report is submitted to the Executive Board for review and discussion. A summary of the Board's views is transmitted to the country's government. Through this kind of peer review, the global community provides policy guidance and advice to each of its members, and the lessons of international experience are brought to bear on national policies. If the member country agrees, the full Article IV consultation report and a Public Information Notice (PIN), which summarizes the Board discussion, are published on the IMF's Web site, in line with the IMF's transparency policy (see Chapter 5).

Supplementing these systematic and regular Board reviews of individual member countries are Executive Board assessments of economic developments and policies in member countries borrowing from the IMF, as well as frequent informal sessions at which the Board discusses developments in individual countries. On a voluntary basis, countries may also choose to participate in the joint Fund-Bank Financial Sector Assessment Program (FSAP) or to request Reports on the Observance of Standards and Codes (ROSCs; Box 2.3).

1 *Appendix II, "Financial operations and transactions," to this* Report *contains a brief summary of members' exchange rate regimes in Table II.9, "De facto classification of exchange rate regimes and monetary policy framework." The Appendix can be found on the CD-ROM and on the IMF's Web site, at* www.imf.org/external/pubs/ft/ar/2007/eng/index.htm.

2 *The IMF's Articles of Agreement can be found at* www.imf.org/external/pubs/ft/aa/index.htm.

Box 2.2 Monetary and Capital Markets Department

Following up on the recommendations in the November 2005 report of the External Review Group on the Organization of Financial Sector and Capital Markets Work at the Fund (experts commissioned by IMF management), the Monetary and Capital Markets Department (MCM) was created in early FY2007.[1] MCM, a merger of the International Capital Markets and the Monetary and Financial Systems departments, centralizes the responsibilities, functions, and expertise of those two departments within a new organizational structure and serves as a resource for other Fund departments.

MCM is responsible for policy, analytical, and technical work relating to financial sectors and capital markets, and monetary and foreign exchange systems, arrangements, and operations. Its principal tasks are to identify potential risks to global financial and macroeconomic stability and their implications for individual countries; assess the vulnerability or soundness of countries' monetary and financial systems and the effective-ness of member governments' oversight of these systems; promote safeguards for the prevention of financial crises and contribute to the operation of the international architecture of risk mitigation and management; and support capacity building in member countries. MCM's capacity-building activities are described in Chapter 4.

1 See Press Release 06/21, at www.imf.org/external/np/sec/pr/2006/pr0621.htm.

Implementing Surveillance

Surveillance focused on several key issues in FY2007, including heightened volatility in financial markets; the potential spillovers and risks associated with a disorderly unwinding of global imbalances; the possible impact of the slowdown in the U.S. housing market on the global economy; and the effect of high prices for oil and other commodities on both importing and exporting countries. The analytical tools used in the preparation of the *World Economic Outlook* and the *Global Financial Stability Report* were applied to capture cross-country spillovers and draw policy lessons.

Global surveillance

World Economic Outlook

In its August 2006 and March 2007 discussions of the *World Economic Outlook* (WEO), the Executive Board welcomed the continued strong, broad-based expansion of the global economy during calendar year 2006, noting that activity in most regions met or exceeded expectations. Executive Directors believed that the global expansion would slow only modestly in 2007 and 2008 and that inflationary pressures would remain contained. They were generally of the view that the market turbulence of February and March 2007 repre-sented a correction after a period of asset price buoyancy that did not require a fundamental revision in the positive global economic outlook.

At the time of the March 2007 discussion, risks to the global economy—the ongoing correction in the U.S. housing market, persistently higher financial market volatility, the chance of a reversal of the decline in oil prices, and the possibility of a disorderly unwinding of large global imbal-ances—were still seen as tilted to the downside but appeared to be more evenly balanced than they had been six months earlier. The key question in assessing these risks is whether the world economy will remain on a sound growth trajectory even if the U.S. economy slows more sharply—that is, whether global prospects might decouple from the United States, especially in view of the limited impact of the recent cooling of U.S. activity.[10]

Global Financial Stability Report

At their March 2007 discussion of the *Global Financial Stability Report* (GFSR), Executive Directors agreed that global financial and macroeconomic stability continued to be underpinned by solid economic prospects, although downside risks had increased somewhat in a few areas. A number of market developments warranted increased attention, reflecting a shift in underlying financial risks and conditions since the Board's discussion of the previous GFSR in August 2006. While none of the identified short-term risks constituted, in and of itself, a threat to financial and macroeconomic stability, adverse events in one area could lead to a reappraisal of risks in other areas, with possible broader implications for the economy. The market turbulence of February and March

10 The full summings up of the Board discussions on the WEO are on the CD-ROM.

2007 validated this assessment and served to remind market participants that such reevaluations could occur quite rapidly. Macroeconomic risks as well as risks faced by emerging markets had eased marginally since the previous GFSR, but market and credit risks had risen, albeit from relatively low levels, and large capital inflows to a number of emerging market countries posed challenges to policymakers. The risks of a disorderly unwinding of global imbalances had also eased somewhat but remained a concern.

Hedge funds were playing a constructive role in improving market efficiency and stability, but the Board cautioned that their size and complex risk structure could lead to increased transmission or amplification of shocks. While observing that the increased diversity of assets, source countries, and investor types contributed to a globalized financial system that, by allowing capital to flow freely, should enable a more effective diversification of risks, enhance the efficiency of capital markets, and support financial and macroeconomic stability, the Board underscored the importance of gradual and carefully sequenced liberalization of financial markets. They welcomed the GFSR's contribution to financial sector surveillance, including in encouraging national legal, regulatory, and supervisory systems to adjust to the more globalized financial environment. Executive Directors favored improved mechanisms for multilateral collaboration, specifically for strengthening supervisory coordination, including through better application of well-established international standards and further work on crisis management and resolution arrangements.[11]

First multilateral consultation

In his April 2006 Report on Implementing the Fund's Medium-Term Strategy, the IMF's Managing Director proposed that existing IMF surveillance arrangements be complemented by a new vehicle—multilateral consultations—that would foster cooperation by appropriate groups of countries on policy actions to address challenges to the global economy and individual members. The proposal was endorsed by the International Monetary and Financial Committee (IMFC), the ministerial-level committee that provides the IMF with policy guidance (see Chapter 5, "How the IMF is run").

The IMF's first multilateral consultation has given its five participants—China, the euro area, Japan, Saudi Arabia, and the United States—a forum for discussing global imbalances and how best to reduce them while sustaining robust global growth. The Executive Board will review the experience with the first multilateral consultation in FY2008.

Commodity prices

Because fluctuations in both oil and nonfuel commodity prices have important policy implications, the IMF has been increasing its coverage of these markets in multilateral surveillance. The Board has consistently advised oil-importing countries, for example, on the importance of market-based pricing—that is, putting an end to subsidies and allowing the pass-through of oil prices to consumers. A chapter in the September 2006 WEO was devoted to nonfuel commodities—metals as well as food and other agricultural commodities—while considerable attention in both the September 2006 and the April 2007 WEO was given to the analysis of the oil market and the effects of oil price changes on the global economy. In their discussions of the WEO, Executive Directors recognized the possibility that inflationary pressures could revive as resource utilization constraints start to bind. They observed that sharply rising prices of nonfuel commodities, particularly metals, had underpinned strong growth in many emerging market and developing countries and advised

Worker in oil field, Zhangaozen, Kazakhstan

11 The full summings up of the Board discussions on the GFSR are on the CD-ROM.

Box 2.3 ROSCs and Data Standards Initiatives

Reports on the Observance of Standards and Codes (ROSCs). Member countries can request ROSCs, assessments of their observance of standards and codes, in any of the following 12 areas: accounting; auditing; anti–money laundering and combating the financing of terrorism (AML/CFT); banking supervision; corporate governance; data dissemination; fiscal transparency; insolvency and creditor rights; insurance supervision; monetary and financial policy transparency; payments systems; and securities regulation. The reports—about 76 percent of which have been published—are used to help sharpen Fund and World Bank policy discussions with national authorities and to strengthen national capacity to participate in, and benefit from, the globalized economy. They are also used in the private sector (including by rating agencies) for risk assessment. Participation in the Standards and Codes Initiative continues to grow. As of end-April 2007, 811 ROSC modules had been completed for 137 countries, or 74 percent of the Fund's membership, and most systemically important countries had volunteered for assessments. More than 380 of the ROSCs were on financial sector standards. Of these, about one-third were related to banking supervision, and the others were fairly evenly distributed across the other standards and codes.

Special Data Dissemination Standard (SDDS). Created in 1996 by the Executive Board, the SDDS is a voluntary standard whose subscribers—countries with access to international capital markets or seeking it—commit to meeting internationally accepted norms of data coverage, frequency, and timeliness. SDDS subscribers provide information about their data compilation and dissemination practices (metadata) for posting on the IMF's Dissemination Standards Bulletin Board (DSBB).[1] Each subscriber is also required to maintain a Web site that disseminates the actual data and that is electronically linked to the DSBB. SDDS subscribers began disseminating prescribed data on external debt in September 2003; data for 58 countries are published in the World Bank's *Quarterly External Debt Statistics* (QEDS). Moldova and Luxembourg became subscribers in FY2007, raising the number of SDDS subscribers to 64 as of April 30, 2007.

General Data Dissemination System (GDDS). The Executive Board established the GDDS in 1997 to help IMF member countries improve their statistical systems. The 88 participants in the GDDS at end-April 2007 provide metadata describing their data compilation and dissemination practices, as well as detailed plans for improvement, for posting on the IMF's DSBB. Between the Executive Board's sixth review of the Data Standards Initiatives in November 2005 and April 30, 2007, eight countries and territories began participating in the GDDS. Of the 94 countries and territories that have participated in the GDDS since it was introduced, 6 have graduated to the SDDS.

To complement the SDDS and GDDS, IMF staff have launched the **Statistical Data and Metadata Exchange (SDMX)** initiative and the **Data Quality Assessment Framework (DQAF).** The SDMX, which is being developed in collaboration with other international organizations, aims to make electronic exchange and management of statistical information among national and international entities more efficient by providing standard practices, coherent protocols, and other infrastructural blueprints for reporting, exchanging, and posting data on Web sites. The DQAF is an assessment methodology that was integrated into the structure of the data ROSCs following the fourth review of the Data Standards Initiatives in 2001.

1 *The Web site address is* dsbb.imf.org/Applications/web/dsbbhome.

these countries to save or invest current revenue windfalls to support future growth in noncommodity sectors. They also stressed the risk of a reversal of the recent decline in oil prices given continuing geopolitical tensions and limited spare production capacity.

The international community is working to improve the quality and transparency of oil market data. In this context, the IMF is increasing the provision of metadata in the General Data Dissemination System and the Special Data Dissemination Standard (see "Standards and codes, including data dissemination" on page 26 and Box 2.3 above). In responding to extensive demand for better data, the IMF is sharing its expertise in data-quality assessment with other international organizations and collaborating with major oil exporters in resolving oil-related data issues. The IMF has also participated in training on the Joint Oil Data Initiative (JODI).[12]

Country surveillance

In FY2007, the Board completed 134 Article IV consultations (see CD-Table 2.1 on the CD-ROM). Country surveillance is becoming more focused on identifying the most important risks facing members and on topics that are core to the IMF's mandate. As an approach for cases in which it appeared useful to concentrate on a few key issues, and in keeping with the MTS's calls for enhancing the efficiency of Fund procedures, the IMF experimented with streamlined consultations with 10 countries during FY2007 to allow additional resources to be devoted to areas of priority work. The Board plans to review the IMF's experience with the streamlined consultations early in FY2008.

As discussed in detail below, considerable work was undertaken in FY2007 to modernize the framework for IMF surveillance and to integrate the analysis of developments in the financial sector and capital markets more fully into country surveillance. Recent efforts have also focused on a deeper examination of cross-country spillovers. As demonstrated by a stocktaking of the quality of exchange rate surveillance (see below), these efforts are gradually bearing fruit.

The IMF's Global Fiscal Model[13] has been used in the context of country surveillance, notably to evaluate the broader impacts of fiscal policy changes—including fiscal consolidation, tax reform, and social security reform—in a number of industrial and emerging market countries. The WEO's analysis of the impact of a slowdown in the U.S. economy on the rest of the world used a variety of econometric and modeling approaches to assess cross-country spillovers.

Regional surveillance and outreach

Since members of currency unions have devolved responsibilities over monetary and exchange rate policies—two central areas of Fund surveillance—to regional institutions, the IMF holds discussions with representatives of these institutions in addition to its Article IV consultations with the unions' individual members. In response to guidance by the Executive Board under the Medium-Term Strategy, IMF staff also conduct other regional surveillance activities, including the production of semiannual regional economic outlooks (REOs), dialogues with various regional forums, and research on issues in which countries in the same region share an interest; and more systematically apply relevant findings of regional surveillance in conducting Article IV consultations. Selected papers and reports increasingly focus on regional spillovers and cross-country experiences.

During FY2007, the IMF's Executive Board discussed developments in the Central African Economic and Monetary Community (CEMAC), the Eastern Caribbean Currency Union (ECCU), the euro area, and the West African Economic and Monetary Union (WAEMU).[14]

12 *Following a period of exceptional volatility in oil prices in the 1990s, in 2001 six international organizations—Asia-Pacific Economic Cooperation (APEC), Eurostat, the International Energy Agency (IEA), Organización Latinoamericana de Energia (OLADE), OPEC, and the United Nations Statistics Division (UNSD)—launched the initiative, originally called the Joint Oil Data Exercise, to raise awareness of the need for more data transparency in oil markets. More information can be found on JODI's Web site, at* www.jodidata.org/FileZ/ODTmain.htm.

13 *The Global Fiscal Model (GFM) is a multicountry general equilibrium model developed at the Fund based on the New Open Economy Macroeconomics (NOEM) tradition, but designed to examine fiscal policy issues. It is particularly suitable for studying temporary or permanent changes in taxes or expenditures, whether occurring rapidly or gradually (as in the case of age-related expenditure pressures). The multicountry feature of the GFM allows the analysis of international spillover effects as changes in government debt influence world interest rates. The GFM also permits practitioners to assess the macroeconomic effects of a number of alternative fiscal-consolidation strategies.*

14 *The summings up of these Board discussions can be found on the CD-ROM and on the IMF's Web site: PIN 06/90, "IMF Executive Board Concludes 2006 Discussion on Common Policies of Member Countries with CEMAC,"* www.imf.org/external/np/sec/pn/2006/pn0690.htm; *PIN 07/13, "IMF Executive Board Concludes 2006 Regional Discussions with Eastern Caribbean Currency Union,"* www.imf.org/external/np/sec/pn/2007/pn0713.htm; *PIN 06/86, "IMF Executive Board Discusses Euro Area Policies,"* www.imf.org/external/np/sec/pn/2006/pn0686.htm; *and PIN 07/55, "IMF Executive Board Concludes 2007 Consultation with West African Economic and Monetary Union,"* www.imf.org/external/np/sec/pn/2007/pn0755.htm.

CEMAC. At their July 2006 discussion, Executive Directors commended CEMAC's positive macroeconomic performance in 2005, which was due in part to oil windfalls and improved implementation of macroeconomic policies. Per capita income in most CEMAC members remains low, however, and these countries face significant challenges in meeting the Millennium Development Goals. The Board urged the authorities to take advantage of improved macroeconomic and financial conditions to address long-standing structural issues that are critical for raising non-oil growth and employment and reducing poverty. They also noted the potential for regional integration to increase market size and foster growth and called for a renewed focus on the promotion of trade. CEMAC participated in an FSAP (see below), which found that financial sector soundness had improved but that important challenges remained. Executive Directors urged CEMAC countries to further strengthen financial and macroeconomic stability and accelerate reforms, particularly as the financial sectors in the region are among the least developed in the world.

ECCU. The Board welcomed the resurgence in economic activity in recent years, driven by tourism, preparations for the Cricket World Cup, and a pickup in private investment. ECCU's quasi-currency-board arrangement has resulted in a long period of price stability, and the currency appears competitive. The challenge will be to sustain the growth momentum in 2007 and beyond. The ECCU countries, which are oil importers, continue to face significant obstacles, including elevated world energy prices and a heavy public debt burden, and exporters of sugar and bananas will need to adjust to the erosion of trade preferences. Further regulatory, administrative, and legal reforms are needed to remove impediments to private business activity. Executive Directors urged continued strengthening of the supervisory and regulatory environment that supports financial market development.

Euro area. Growth has picked up and broadened in the euro area, the reformed Stability and Growth Pact is regaining traction over fiscal policies, fiscal outcomes have been better than originally projected, and progress has been made in the reform of product and services markets and financial integration. However, the Board saw risks tilting to the downside for 2007 and beyond. Productivity growth continues to be sluggish, employment and consumption continue to lag, oil prices are volatile, and global imbalances remain unresolved. Executive Directors underscored the need for accelerated fiscal consolidation and further structural reforms that aim at strengthening incentives to work and invest.

WAEMU. The overall economic situation in WAEMU was challenging in 2006. Inflation fell sharply despite higher prices for fuel imports, and foreign reserve levels remained adequate, but average growth declined to 3.4 percent and the current account deficit widened. Progress on policy convergence, economic integration, and structural reforms has been slow, and growth and deeper regional integration are hampered by macroeconomic shocks, structural weaknesses, and, in some countries, sociopolitical problems. However, WAEMU is stepping up efforts to remove these obstacles. In 2006, it embarked on trade reform and instituted an ambitious reform program for 2006–10. Given that the region's financial sector is unintegrated and shallow, the Board welcomed the authorities' request for a regional FSAP.

Regional Economic Outlooks (REOs) are produced semiannually for sub-Saharan Africa, Asia and the Pacific, the Middle East and Central Asia, and the Western Hemisphere.[15] Upon publication of the REOs, the IMF organizes press conferences or seminars at headquarters or in the field. Area department staff often go on road shows to present REO findings at different venues to diverse audiences in the region in question. The Middle East and Central Asia Department, for example, organizes outreach activities in association with its REOs twice a year in Dubai, Central Asia, and North Africa.

Intensified outreach has contributed to wider dissemination of the findings of IMF studies and stimulated debate on regional issues. In addition to the activities undertaken in connection with the publication of the REOs, the Fund organizes regional conferences and seminars either on its own or in collaboration with regional entities. (For examples, see the section on outreach in Chapter 5.)

15 *The full text of these reports can be found on the IMF's Web site, at* www.imf.org. *There are plans to publish a* Regional Economic Outlook *for Europe beginning in the fall of 2007.*

The Bovespa stock exchange, São Paulo, Brazil

Financial sector surveillance and the Standards and Codes Initiative

For countries to reap the full benefit of cross-border capital flows, which have increased dramatically over the past two decades, their financial sectors must be resilient and well regulated. In 1999, the IMF and the World Bank introduced a joint initiative, the FSAP, to provide member countries, on a voluntary basis, with a comprehensive evaluation of their financial systems. The FSAP, a cornerstone of financial sector surveillance, provides the basis for the IMF's Financial System Stability Assessments (FSSAs)—assessments of risks to macroeconomic stability stemming from the financial sector, including the latter's ability to absorb macroeconomic shocks.

Regional FSAPs can be undertaken for currency unions, notably where significant regulatory and supervisory structures are at the regional level. As described above, a regional FSAP—for CEMAC—was completed in FY2007, and WAEMU requested an FSAP. In addition, the IMF has undertaken regional financial sector projects in Central America, the Maghreb, and the Nordic-Baltic region.[16]

With a total of 123 initial assessments now completed or under way, the IMF and the World Bank are increasingly focusing on FSAP updates. The core elements of updates include financial stability analysis, factual updates of the observance of standards and codes included in the initial assessment,[17] and reexamination of key issues raised in the initial assessment. Updates usually require only a single visit by an IMF–World Bank team (initial assessments require two)—and a smaller team—and hence are typically less resource-intensive than initial assessments.

In FY2007, 18 FSAPs were completed, of which 6 were updates;[18] another 53 (of which 30 are updates) are either under way or agreed and being planned.

16 *See Box 3.4, "Regional financial integration in Central America," in the IMF's* Annual Report 2006, *at* www.imf.org/external/pubs/ft/ar/2006/eng/index.htm.
17 *Factual updates describe developments that are relevant to compliance with standards and codes but do not reassess the ratings in the initial FSAP.*
18 *These numbers refer to FSSAs discussed by the Board during FY2007.*

Work is progressing on incorporating a financial sector component into the IMF's Global Economy Model.[19] The IMF is also studying both the implications of growing international financial integration for national fiscal policies and the linkages between the financial sector and fiscal institutions and policy.

Standards and codes, including data dissemination

In the wake of the Asian crisis of 1997–98, during their discussions on strengthening the international financial architecture, Executive Directors stressed the need to develop and implement internationally recognized standards and codes of good practice that would foster financial and macroeconomic stability at both the domestic and the international levels. The result was the launch of the Standards and Codes Initiative in 1999. The IMF and the World Bank evaluate member countries' policies against international benchmarks of good practice in three broad areas—transparent government operations and policymaking, financial sector standards, and market integrity standards for the corporate sector—and issue Reports on the Observance of Standards and Codes (ROSCs; see Box 2.3), which are intended to help countries strengthen their economic institutions, to inform the work of the IMF and the Bank, and to inform market participants. Following up on the Executive Board's review of the Standards and Codes Initiative in FY2006 and the recommendations of the MTS, the Initiative has been strengthened, with clearer country prioritization of ROSCs and updates, better integration of ROSCs with surveillance and technical assistance, and greater clarity of ROSCs. Several standards have been revised in recent years, and the revised standards are now being used as the basis for assessments. For example, in April 2007, the Board endorsed the new Basel Core Principles[20] standard and methodology released in October 2006.

Since the Asian crisis of 1997–98, the analysis of balance sheet vulnerabilities has become an increasingly important part of country risk assessment at the IMF.

Underpinning assessments of fiscal transparency in 86 countries under the Standards and Codes Initiative is the IMF's *Code of Good Practices on Fiscal Transparency,* which was revised during FY2007, after a broad public consultation process. The Code, launched in 1998, is a central element in the IMF's efforts to help members implement standards in the areas of transparency and good governance. Fiscal transparency leads to better-informed public debate about fiscal policy, makes governments more accountable for policy implementation, and strengthens government credibility, thereby strengthening countries' capacity for sound macroeconomic policymaking, public debt management, and budget preparation.[21] A major aim of the revised Code is to fully integrate issues related to resource-revenue transparency, drawing on experience gained from use of the IMF's 2005 *Guide on Resource Revenue Transparency,* which focuses on the problems of countries that derive a significant share of their revenues from hydrocarbon and mineral resources. The revised Code also extends the coverage of good practice to address more explicitly some key fiscal transparency issues, such as fiscal risk management, the openness of budgets and policy decisions, external audit processes, and the publication of a citizens' guide to the budget. Extensive revisions have also been made to the *Manual on Fiscal Transparency,* which provides detailed guidance on good fiscal transparency practices, with examples from a range of developing, emerging, and advanced economies.[22]

19 *The Global Economy Model (GEM), which the IMF has been developing since 2002, is a large, multicountry macroeconomic model based on an explicit microeconomic framework in which consumers maximize utility and producers maximize profits. The integration of domestic supply, demand, trade, and international asset markets in a single theoretical structure allows transmission mechanisms to be fully articulated, providing new insights not obtainable from earlier models. A range of GEM simulations have been used in IMF work to assess issues such as the domestic and international consequences of policies to increase competition in markets, the impact of oil price increases, the effects on emerging market countries of exchange rate volatility across industrial countries, and appropriate monetary policy rules for emerging market countries. A detailed description of the model can be found at* www.imf.org/external/np/res/gem/2004/eng/index.htm.

20 *The* Core Principles for Effective Banking Supervision, *which the Basel Committee on Banking Supervision originally published in September 1997, were updated in 2006 to keep pace with changes in banking regulation. The Core Principles and the* Core Principles Methodology *are used by countries as a benchmark for assessing the quality of their supervisory systems and for identifying future work that needs to be done to overcome regulatory and supervisory shortcomings. The IMF and the World Bank also use the Core Principles in the context of the Financial Sector Assessment Program to assess countries' banking supervision systems and practices.*

21 *The Code can be found at* www.imf.org/external/np/fad/trans/code.htm.

22 *Available at* www.imf.org/external/np/fad/trans/manual/index.htm.

In addition, in September 2006 the IMF began publishing *International Financial Statistics, Supplement on Monetary and Financial Statistics, Supplement Series No.17,* a quarterly compilation of monetary and financial statistics for 65 countries. These data are an important input for compiling the matrices of the IMF's balance sheet approach to assessing debt vulnerabilities. Since the Asian crisis, the analysis of balance sheet vulnerabilities has become an increasingly important part of country risk assessment at the IMF. Information about balance sheets in a country's key economic sectors (public, private financial and nonfinancial, and household and nonresident) facilitates assessments of maturity, currency, and capital structure mismatches as well as intersectoral linkages.

In view of the evolving economic environment and changing needs for economic analysis, the IMF is updating macroeconomic statistical standards in close collaboration with member countries and other international organizations. The IMF is contributing to the update of the System of National Accounts 1993, and it has drafted and posted on its Web site for worldwide consultation the sixth edition of the *Balance of Payments and International Investment Position Manual* and the *Export and Import Price Index Manual.* The update of the various statistical standards is being coordinated to ensure maximum harmonization of statistical methodologies. The methodological standards in statistics underpin the IMF's work on data ROSCs, technical assistance, and training, and promote the comparability of data and best practices in statistical methodology.

Modernizing the Surveillance Framework and Integrating Financial Sector Analysis

Over the past 30 years, the Executive Board has reviewed the IMF's surveillance work at regular intervals. From 1988 to 2004, reviews were conducted biennially. A decision was made in 2006 to move to triennial reviews in accordance with the MTS's call for streamlining IMF procedures. The most recent

Currency exchange board, Bangkok, Thailand

review, conducted in 2004, called for deeper treatment of exchange rate issues, including (1) clear identification of the de facto exchange rate regime in staff reports, (2) more systematic use of a broad set of indicators and analytical tools to assess external competitiveness, and (3) a thorough and balanced presentation of the policy dialogue between the staff and the authorities on exchange rate issues.[23] Following up on these recommendations, in August 2006, the Executive Board discussed a paper by IMF staff assessing the quality of recent work by the IMF on exchange rate issues in 30 large economies accounting for more than 90 percent of world GDP.[24] Executive Directors generally agreed that exchange rate surveillance had improved appreciably since the 2004 review and that the quality of the analysis was mostly adequate in three of the four dimensions reviewed—the description of the exchange rate regime, the assessment of the regime, and the consistency of exchange rate policies with external stability—

23 *The Biennial Surveillance Review can be found on the IMF's Web site, at* www.imf.org/external/np/sec/pn/2004/pn0495.htm.

24 *The paper, "Treatment of Exchange Rate Issues in Bilateral Fund Surveillance—A Stocktaking," can be found on the IMF's Web site, at* www.imf.org/external/pp/longres.aspx?id=3951. *The summing up of the Board discussion can be found on the CD-ROM and on the IMF's Web site: PIN 06/131, "IMF Executive Board Discusses Treatment of Exchange Rate Issues in Bilateral Surveillance—A Stocktaking,"* www.imf.org/external/np/sec/pn/2006/pn06131.htm.

The IMF Executive Board has strengthened surveillance over exchange rate policies and called for greater scrutiny of the linkages between the financial sector and the macroeconomy.

but that there was room for better analysis in the fourth, the assessment of exchange rate levels and external competitiveness. The Board also called for a greater focus on the spillover effects of countries' exchange rate policies.

As part of the effort to strengthen the IMF's framework for assessing exchange rate issues, at an informal seminar in November 2006, the Executive Board discussed a staff report on revised and extended methodologies for exchange rate assessments by the IMF's Consultative Group on Exchange Rate Issues (CGER). The CGER, which has provided exchange rate assessments for a number of advanced economies since the mid-1990s, has extended its methodologies to cover about 20 emerging market countries. These methodologies can help gauge the consistency of current account balances and real effective exchange rates with their underlying fundamentals. Staff organized outreach events with officials, academics, and market participants in Europe, Asia, and Africa to discuss this extension and approaches to exchange rate modeling.[25]

Complementing the periodic efforts of the Executive Board and the Fund's management and staff to take stock of the effectiveness of surveillance, the IMF's Independent Evaluation Office (IEO; see Box 5.3) completed an evaluation in FY2007 of the IMF's exchange rate policy advice, for discussion by the Executive Board in early FY2008.[26] The IEO set out to answer three main questions: Is the role of the IMF clearly defined and understood? How good is the quality of the IMF's advice and its underlying analysis? And how effective is the IMF in its policy dialogue with country authorities? Its report acknowledges that the quality of the IMF's advice to its member countries had improved in some ways from 1999 to 2005, citing many examples of good analysis and dedicated staff teams. At the same time, it identifies a need to revalidate the fundamental purpose of IMF exchange rate surveillance and thus clarify the expected roles of the IMF and member countries, offering detailed recommendations for improving the management and conduct of the IMF's exchange rate policy advice and interactions with member countries.

The principles and procedures governing the scope and operational modalities of surveillance over exchange rate policies were adopted by the Executive Board in 1977, after the collapse of the Bretton Woods system of fixed exchange rate parities.[27] In FY2007, the Board held discussions on the possibility of revising the Decision to broaden it to cover surveillance more comprehensively, and to align it more closely with Article IV and current best practice.[28] A revised decision would not only demonstrate the Fund's resolve to strengthen the effectiveness of surveillance, including over exchange rates, but also serve as a basis for the practice of surveillance, unifying guidance, clarifying issues and procedures, and providing a better foundation for surveillance to address priority issues. In their discussion, Executive Directors found important areas of broad agreement and subsequently worked to build common ground on other areas. At the Spring Meetings of the IMF and the World Bank, the IMFC agreed that the following principles should guide further work: (1) there should be no new obligations, and dialogue and persuasion should remain key pillars of effective surveillance; (2) surveillance should pay due regard to country circumstances and emphasize the need for evenhandedness; and (3) a revised decision should be flexible enough to allow surveillance to evolve as circumstances warrant.[29]

25 *See Press Release 06/266, "IMF Strengthening Framework for Exchange Rate Surveillance," on the CD-ROM or at* www.imf.org/external/np/sec/pr/2006/pr06266.htm.

26 *The IEO's report can be found at* www.ieo-imf.org/eval/complete/eval_05172007.html.

27 *The 1977 Decision on Surveillance over Exchange Rate Policies can be found on the IMF's Web site, at* www.imf.org/external/pubs/ft/sd/index.asp?decision=5392-(77/63).

28 *See "Article IV of the Fund's Articles of Agreement: An Overview of the Legal Framework," a paper prepared by IMF staff, at* www.imf.org/external/np/pp/eng/2006/062806.pdf.

29 *On June 15, 2007, after the end of the financial year, the Board adopted the 2007 Decision on Bilateral Surveillance over Members' Policies, which replaces the 1977 Decision. The summing up of the Board discussion can be found at* www.imf.org/external/np/sec/pn/2007/pn0769.htm.

During FY2007, the Board also exchanged views on the possibility of introducing a clear statement of surveillance priorities to guide implementation and facilitate ex post monitoring of effectiveness (a "remit"), against the background of the existing accountability and independence framework. In doing so, it examined methods for assessing the effectiveness of IMF surveillance and agreed that a strengthened methodology should be introduced in the context of the next review of surveillance, scheduled to take place in FY2008.

Integrating financial sector and capital markets analysis into surveillance

A task force was established in FY2006 to study the issue of how to better integrate the IMF's financial sector work into its surveillance. The task force delivered its recommendations in FY2007, emphasizing the need for a broader multilateral perspective, more focus on the financial sector's impact on growth and the macroeconomy, and a thorough assessment of risks. Following up on these recommendations, the IMF has increased interdepartmental cooperation and prioritized its financial sector work, with heightened monitoring of both systemically important countries and countries vulnerable to crisis.

The IMF also contributes to international efforts to combat money laundering and the financing of terrorism, in collaboration with the Financial Action Task Force on Money Laundering (FATF), the World Bank, the United Nations, and FATF-style regional bodies (FSRBs). As a collaborative institution with near universal membership, the IMF is a natural forum for sharing information, developing common approaches to issues, and promoting desirable policies and standards. In addition, the IMF's broad experience in conducting financial sector assessments, providing technical assistance in the financial sector, and exercising surveillance over members' economic systems is particularly valuable in evaluating country compliance with international AML/CFT standards and in developing programs to help them address shortcomings. In 2004, the Executive Board agreed to make AML/CFT assessments and technical assistance a regular part of Fund work and to expand this work to cover the full scope of the FATF's 40 recommendations designed to guide national policymakers in implementing effective anti–money laundering programs and 9 additional recommendations on combating the financing of terrorism.

In its June 2006 discussion of a paper jointly prepared by IMF and World Bank staff on the quality and consistency of assessments of national AML/CFT regimes,[30] which are carried out by the IMF, the World Bank, the FATF, or the FSRBs, using an agreed common methodology, the Executive Board reiterated the importance of AML/CFT in strengthening the integrity of financial systems and deterring financial abuse and confirmed the IMF's collaborative arrangements with the FATF and FSRBs for assessing AML/CFT regimes. As part of its review, the Executive Board examined the findings of an expert panel that had analyzed a sample of AML/CFT assessments prepared by different bodies and concluded that there was a high degree of variability in the quality and consistency of the reports. The Executive Board noted that a number of initiatives had been taken or were under way to improve the assessments and called on IMF staff to provide technical assistance to, and cooperate more closely with, the FSRBs.

The Board also agreed that every assessment or update under the FSAP or Offshore Financial Center (OFC) assessment program[31] should include a full AML/CFT assessment using the most recent methodology and that full AML/CFT assessments should be conducted approximately every five years. The Fund is expected to continue monitoring significant financial sector problems arising from money laundering or terrorism-financing activities through other vehicles, such as assessments of other financial sector standards, Article IV consultations, and participation in FATF and regional forums.

The Executive Board has consistently underscored the importance of financial soundness indicators (FSIs) in facilitating financial sector surveillance, increasing the transparency and stability of the international financial

30 *The staff paper is available at* www.imf.org/external/np/pp/eng/2006/041806r.pdf. *The summing up of the Board's discussion can be found on the CD-ROM and on the IMF's Web site, at* www.imf.org/external/np/sec/pn/2006/pn0672.htm.

31 *The OFC assessment program was initiated in 2000. The monitoring of OFCs, to ensure their compliance with supervisory and integrity standards, has become a standard component of the IMF's financial sector work.*

system, and strengthening market discipline. After developing a core set and an encouraged set of FSIs in consultation with the international community, the IMF launched the three-year pilot Coordinated Compilation Exercise (CCE), which was endorsed by the Board, in March 2004 to (1) build the capacity of the 62 participating countries to compile FSIs; (2) promote cross-country comparability of FSIs; (3) coordinate efforts by national authorities to compile FSIs; and (4) disseminate the FSI data compiled in the CCE, along with metadata, to increase transparency and strengthen market discipline. The methodology recommended by the IMF to ensure cross-country comparability is presented in the *Financial Soundness Indicators: Compilation Guide*.[32] By the end of FY2007, FSI data and metadata for 52 of the 62 countries participating in the CCE were posted on the IMF's Web site.[33] Many countries also regularly compile and disseminate FSIs on their own, and these indicators are included in FSAP documents.

32 *The Guide can be found at* www.imf.org/external/pubs/ft/fsi/guide/2006/index.htm. *The list of core and encouraged FSIs can be found at* www.imf.org/external/np/sta/fsi/eng/fsi.htm.

33 *Another five countries posted their data and metadata in the first month of FY2008; see* www.imf.org/external/np/sta/fsi/eng/cce/index.htm.

Chapter 3

Chapter 3 Program support

The IMF provides financial and other kinds of support to its member countries through a variety of instruments, including lending facilities, tailored to their different circumstances (Table 3.1). Review and approval of members' requests for financial assistance and program support are core responsibilities of the Board, alongside surveillance.

Under the Fund's lending facilities, the Board makes temporary financing available to members to help them address a variety of balance of payments problems, such as a lack of sufficient foreign exchange to purchase needed imports or make payments on external obligations. IMF loans give countries time to adjust their policies so as to overcome short-term balance of payments problems, stabilize their economies, and avoid similar problems in the future. IMF lending is not intended to cover all of a borrower's needs but, rather, to have a catalytic effect—enabling a country to restore confidence in its policies and attract financing from other sources. Loans are accompanied by economic reform programs developed by the borrowers in collaboration with the IMF. The Executive Board regularly reviews borrowers' performance under their programs, and, in most cases, funds are disbursed as program targets are met.

Regular financing activities. The bulk of the IMF's loans are provided through Stand-By Arrangements (SBAs), which address members' short-term balance of payments difficulties, and the Extended Fund Facility (EFF), which focuses on external payments difficulties caused by longer-term structural problems. For members experiencing a sudden and disruptive loss of access to capital markets, these loans can be supplemented with short-term resources from the IMF's Supplemental Reserve Facility (SRF). In addition, special Emergency Assistance is available to countries recovering from conflicts or natural disasters. All of these loans incur interest charges, and many may be subject to surcharges, depending on the type and duration of the loan and the amount of IMF credit outstanding. Repayment periods vary by type of loan. The IMF's regular lending activities are financed out of a revolving pool of funds held in the General Resources Account (GRA) and consisting mainly of members' quota subscriptions. In addition, the IMF has in place two formal borrowing arrangements with member countries and can borrow to supplement its quota resources.

Financing for low-income countries. The IMF provides support to its low-income members through a variety of instruments. These include highly subsidized lending through the Poverty Reduction and Growth Facility (PRGF) and the Exogenous Shocks Facility (ESF); subsidized Emergency Assistance for eligible post-conflict countries and countries hit by natural disasters;[34] and debt relief under the Heavily Indebted Poor Countries (HIPC) Initiative and the Multilateral Debt Relief Initiative (MDRI).[35] The PRGF, the main instrument for provision of IMF financial support to low-income countries, focuses on poverty reduction in the context of a growth-oriented economic strategy, while the ESF provides concessional assistance to low-income members that are facing sudden exogenous shocks but do not have a PRGF arrangement in place. A low-income country seeking a PRGF or ESF loan or debt relief must prepare a Poverty Reduction Strategy Paper (PRSP) in a participatory process involving civil society; the PRSP is considered by the Boards of the IMF and the World Bank, but the strategy is developed and owned by the country. The funds for PRGF loans come from trust funds administered by the IMF, and the subsidy resources are financed by contributions from the IMF and a broad spectrum of its member countries.

Special Drawing Rights. The IMF can create international reserve assets by allocating Special Drawing Rights (SDRs) to members (Box 3.1). Recipient countries can use SDRs to obtain foreign exchange from other members and to make payments to the IMF. SDRs are also the IMF's unit of account.

Box 3.1 Special Drawing Rights

The SDR is a reserve asset created by the IMF in 1969 in response to the threat of a shortage of international liquidity. SDRs are "allocated"—distributed—to members in proportion to their IMF quotas. Since the SDR's creation, a total of SDR 21.4 billion has been allocated to members—SDR 9.3 billion in 1970–72 and SDR 12.1 billion in 1979–81.Today, the SDR has only limited use as a reserve asset. Its main function is to serve as the unit of account of the IMF and some other international organizations and a means of payment for members in settling their IMF financial obligations. The SDR is neither a currency nor a claim on the IMF. Rather, it is a potential claim on the freely usable currencies of IMF members. Holders of SDRs can obtain these currencies in exchange for their SDRs in two ways: first, through the arrangement of voluntary exchanges between members; and second, by the IMF's designating members with strong external positions to purchase SDRs from members with weak external positions in exchange for freely usable currencies.

The value of the SDR is based on the weighted average of the values of a basket of major international currencies, and the SDR interest rate is a weighted average of interest rates on short-term instruments in the markets for the currencies in the valuation basket. The method of valuation is reviewed every five years. The latest review was completed in November 2005, and the IMF Executive Board decided on changes in the valuation basket effective January 1, 2006. The SDR interest rate is calculated weekly and provides the basis for determining the interest charges on regular IMF financing and the interest rate paid to members that are creditors of the IMF.

34 CD-Tables 3.1 and 3.2, which show subsidy contribution pledges as of April 30, 2007, for the ESF and for Emergency Assistance, respectively, can be found on the CD-ROM.

35 The HIPC Initiative was launched by the IMF and the World Bank in 1996 and enhanced in 1999 to provide faster, deeper, and broader debt relief and to strengthen the links between debt relief, poverty reduction, and social policies. CD-Tables 3.3 and 3.4, which show the delivery of debt relief as of April 30, 2007, can be found on the CD-ROM. More information about the HIPC Initiative can be found on the IMF's Web site, at www.imf.org/external/np/exr/facts/hipc.htm.

Table 3.1 IMF lending facilities

Credit facility (year adopted)	Purpose	Conditions	Phasing and monitoring[1]
Credit tranches and Extended Fund Facility[4]			
Stand-By Arrangements (1952)	Medium-term assistance for countries with balance of payments difficulties of a short-term character.	Adopt policies that provide confidence that the member's balance of payments difficulties will be resolved within a reasonable period.	Quarterly purchases (disbursements) contingent on observance of performance criteria and other conditions.
Extended Fund Facility (1974) (Extended Arrangements)	Longer-term assistance to support members' structural reforms to address balance of payments difficulties of a long-term character.	Adopt 3-year program with structural agenda, with annual detailed statement of policies for the next 12 months.	Quarterly or seminannual purchases (disbursements) contingent on observance criteria and other conditions.
Special facilities			
Supplemental Reserve Facility (1977)	Short-term assistance for balance of payments difficulties related to crises of market confidence.	Available only in context of Stand-By or Extended Arrangements with associated program and with strengthened policies to address loss of market confidence.	Facility available for one year; front-loaded access with two or more purchases (disbursements).
Compensatory Financing Facility (1963)	Medium-term assistance for temporary export shortfalls or cereal import excesses. .	Available only when the shortfall/excess is largely beyond the control of the authorities and a member has an arrangement with upper credit tranche conditionality, or when its balance of payments position excluding the shortfall/excess is satisfactory.	Typically disbursed over a minimum of six months in accordance with the phasing provisions of the arrangement.
Emergency Assistance	Assistance for balance of payments difficulties related to the following:		None, although post-conflict assistance can be segmented into two or more purchases.
(1) Natural disasters (1962)	Natural disasters	Reasonable efforts to overcome balance of payments difficulties.	
(2) Post-conflict (1995)	The aftermath of civil unrest, political turmoil, or international armed conflict.	Focus on institutional and administrative capacity building to pave the way toward an upper credit tranche arrangement or PRGF.	
Facilities for low-income members			
Poverty Reduction and Growth Facility (1999)	Longer-term assistance for deep-seated balance of payments difficulties of structural nature; aims at sustained poverty-reducing growth.	Adopt 3-year PRGF arrangements. PRGF-supported programs are based on a Poverty Reduction Strategy Paper (PRSP) prepared by the country in a participatory process and integrating macroeconomic, structural, and poverty reduction policies.	Semiannual (or occasionally quarterly) disbursements contingent on observance of performance criteria and reviews.
Exogenous Shocks Facility (2006)	Short-term assistance to address a temporary balance of payments need that is due to an exogenous shock.	Adopt a 1–2 year program involving macroeconomic adjustments allowing the member to adjust to the shock and structural reform considered important for adjustment to the shock, or for mitigating the impact of future shocks.	Semiannual or quarterly disbursements on observance of performance criteria and, in most cases, completion of a review.

1 *Except for the PRGF, the IMF's lending is financed from the capital subscribed by member countries; each country is assigned a* quota *that represents its financial commitment. A member provides a portion of its quota in foreign currencies acceptable to the IMF—or SDRs (see Box 3.1)—and the remainder in its own currency. An IMF loan is disbursed or drawn by the borrower* purchasing *foreign currency assets from the IMF with its own currency. Repayment of the loan is achieved by the borrower* repurchasing *its currency from the IMF with foreign currency. See CD-Box 5.1 on the IMF's financing mechanism. PRGF lending is financed by a separate PRGF-ESF Trust.*

2 The rate of charge *on funds disbursed from the General Resources Account (GRA) is set at a margin over the weekly interest rate on SDRs. The rate of charge is applied to the daily balance of all outstanding GRA drawings during each IMF financial quarter. In addition, a one-time service charge of 0.5 percent is levied on each drawing of IMF resources in the GRA, other than reserve tranche drawings. An up-front commitment fee (25 basis points on committed amounts up to 100 percent of quota, 10 basis points thereafter) applies to the amount that may be drawn during each (annual) period under a Stand-By or Extended Arrangement; this fee is refunded on a proportionate basis as subsequent*

		Repurchase (repayment) terms[3]		
Access limits[1]	Charges[2]	Obligation schedule *(Years)*	Expectation schedule *(Years)*	Installments
Annual: 100% of quota; cumulative: 300% of quota.	Rate of charge plus surcharge (100 basis points on amounts above 200% of quota; 200 basis points on amounts above 300% of quota).[5]	$3\frac{1}{4}$–5	$2\frac{1}{4}$–4	Quarterly
Annual: 100% of quota; cumulative: 300% of quota.	Rate of charge plus surcharge (100 basis points on amounts above 200% of quota; 200 basis points on amounts above 300% of quota).[5]	$4\frac{1}{2}$–10	$4\frac{1}{2}$–7	Semiannual
No access limits; access under the facility only when access under associated regular arrangement would otherwise exceed either annual or cumulative limit.	Rate of charge plus surcharge (300 basis points, rising by 50 basis points a year after first disbursement and every 6 months thereafter to a maximum of 500 basis points).	$2\frac{1}{2}$–3	2–$2\frac{1}{2}$	Semiannual
45% of quota each for export and cereal components. Combined limit of 55% of quota for both components.	Rate of charge.	$3\frac{1}{4}$–5	$2\frac{1}{4}$–4	Quarterly
Generally limited to 25% of quota, though larger amounts of up to 50% can be made available in exceptional cases.	Rate of charge; however, the rate of charge may be subsidized to 0.5 percent a year, subject to resource availability.	$3\frac{1}{4}$–5	Not applicable	Quarterly
140% of quota; 185% of quota in exceptional circumstances.	0.5%	$5\frac{1}{2}$–10	Not applicable	Semiannual
Annual: 25% of quota; cumulative: 50% of quota except in exceptional circumstances.	0.5%	$5\frac{1}{2}$–10	Not applicable	Semiannual

drawings are made under the arrangement.

3 *For purchases made after November 28, 2000, members are expected to make repurchases (repayments) in accordance with the schedule of expectation; the IMF may, upon request by a member, amend the schedule of repurchase expectations if the Executive Board agrees that the member's external position has not improved sufficiently for repurchases to be made.*

4 Credit tranches *refer to the size of purchases (disbursements) in terms of proportions of the member's quota in the IMF; for example, disbursements up to 25 percent of a member's quota are disbursements under the* first credit tranche *and require members to demonstrate reasonable efforts to overcome their balance of payments problems. Requests for disbursements above 25 percent are referred to as* upper credit tranche drawings*; they are made in installments as the borrower meets certain established performance targets. Such disbursements are normally associated with a Stand-By or Extended Arrangement. Access to IMF resources outside an arrangement is rare and expected to remain so.*

5 *Surcharge introduced in November 2000.*

The Fund can also provide loans under its lending facilities through the Trade Integration Mechanism (TIM), which it introduced in FY2004. The TIM is not a lending facility itself, but, rather, a policy. It is designed to help mitigate concerns among some developing countries that their balance of payments positions could suffer, albeit temporarily, as multilateral trade liberalization changes their competitive position in world markets.

Detailed information about the amounts of lending approved by the IMF, credit outstanding, and repayments, broken down by lending facility and financial year, can be found in the Appendix II tables on the CD-ROM.

The IMF's Executive Board frequently reviews and refines the IMF's policies and instruments to ensure that they meet members' evolving needs. During FY2007, the IMF's Executive Board began work on the development of a new contingent financing instrument that emerging market countries active in international capital markets could draw on if they experience a sudden, temporary loss of liquidity. To help low-income countries avoid building up excessive debt after benefiting from debt relief, the Boards of the IMF and the World Bank decided to strengthen the Debt Sustainability Framework (DSF) developed by the two institutions in 2005, and the IMF and the World Bank engaged in outreach on ways to use the DSF more effectively. The Board also reviewed the report of the Independent Evaluation Office (IEO; Box 5.3), "The IMF and Aid to Sub-Saharan Africa," concluded a review of "ex post assessments"—assessments of the successes and failures of IMF-supported programs with repeat or longer-term borrowers—and reviewed the IMF's experience over 1992–2005 with precautionary arrangements, which give countries not facing immediate balance of payments problems the right to draw on financial assistance from the IMF should the need arise, conditional on the implementation of specific policies.

Emerging Market Economies

Many emerging market economies have moved from programs to a surveillance-only relationship with the IMF. As these countries have gained access to international capital markets, they have repaid their IMF loans ahead of schedule and their need for new IMF lending has decreased dramatically.

Lending

IMF credit outstanding at the end of FY2007 declined to SDR 7.3 billion from SDR 19.2 billion in April 2006, owing to continued early repayments of outstanding loans and a low level of new disbursements (Figure 3.1).[36] During FY2007, nine members—Bulgaria, the Central African Republic, Ecuador, Haiti, Indonesia, Malawi, the Philippines, Serbia, and Uruguay—repaid their outstanding obligations to the IMF ahead of schedule, for a total of SDR 7.1 billion. IMF disbursements totaled SDR 2.3 billion, the bulk of which went to Turkey.

Figure 3.1 Regular loans outstanding, FY1997–FY2007

(In billions of SDRs)

Source: IMF Finance Department.

New IMF commitments fell sharply, from SDR 8.3 billion in FY2006 to SDR 237 million in FY2007, with two new Stand-By Arrangements approved for Paraguay and Peru. Seven Stand-By and Extended Arrangements were in effect as of the end of FY2007, of which four are being treated as precautionary since borrowers have indicated their intention not to draw on them. At the end of April 2007, undrawn balances under all current Stand-By and Extended Arrangements amounted to SDR 3.9 billion.

36 The IMF's liquidity, as measured by the Forward Commitment Capacity (FCC), rose to an all-time high of SDR 126.1 billion at the end of April 2007, from SDR 120.1 billion at the end of April 2006, largely because of the significant decline in lending.

New financing instrument

A number of the IMF's members have called for consideration of a new financing instrument designed specifically to support crisis-prevention efforts by members active in international capital markets. As part of the analytical backdrop to the design of such an instrument, in May 2006 the Executive Board held an informal seminar to discuss a study on the role of IMF-supported programs in crisis prevention.[37] Based on theoretical and empirical work, that study found that the availability of IMF resources can have a significant impact on lowering the likelihood of a crisis. Moreover, the marginal impact of IMF support depends on the quality of the member's policies and economic fundamentals—accordingly, the availability of IMF financial resources can have a strong complementary effect to the member's own crisis-prevention efforts. Building on this analytical work, at a seminar in August 2006, the Executive Board discussed the objectives for a new financing instrument, taking into account the IMF's experience with an earlier instrument, the Contingent Credit Lines (CCL).[38]

A successful instrument would reduce the risk of a crisis by granting qualified members—that is, countries following sound policies—access to a credit line, thereby lowering the incentive for private investors to reduce their exposure early, at the first sign of trouble. It would also need to balance predictable access to IMF financing against adequate safeguards for IMF resources, and manage the tension between the provision of strong positive signals when conditions are good and the possibility that entry or exit from the instrument could generate negative signals when circumstances deteriorate.

At the September 2006 Annual Meetings, the IMFC requested that the IMF continue to work on designing a new instrument, tentatively called the Reserve Augmentation Line. Outreach by IMF management and staff with officials and market participants facilitated further work on the instrument's design, and in March 2007 Executive Directors discussed a paper that sought further convergence of views on key design issues, such as qualification, monitoring, access, terms, and a sunset clause.[39] The discussion clarified areas of emerging common ground and revealed areas where further progress is needed. The Executive Board called on IMF staff to prepare a follow-up paper refining the proposals.

Low-Income Countries

The MTS identifies the need to make the IMF's engagement with low-income countries more flexible, as well as more focused on what is essential and on areas where the IMF has a comparative advantage and expertise. Over the past few years, the Board has approved a wide array of instruments to help the IMF's low-income members achieve macroeconomic stability and sustainable growth, which are critical to the achievement of the Millennium Development Goals (Box 3.2). In addition to the advice given to countries in the course of its surveillance activities, the IMF provides advice, financial assistance, and debt relief in connection with the facilities described above, and 90 percent of its technical assistance goes to low- and lower-middle-income countries (see Chapter 4). For low-income countries eligible for PRGF lending that do not want financial assistance from the IMF but do want support of their policies through counsel and advice, the IMF created the Policy Support Instrument (PSI) in FY2006. As of April 30, 2007, four countries had applied for and received PSIs. The Fund also continues to advocate a successful outcome to the Doha Round of trade negotiations (Box 3.3).

Concessional lending

During FY2007, the Executive Board approved 10 new PRGF arrangements (Table 3.2), with commitments totaling SDR 401.2 million. The Board also approved the augmentation of two PRGF arrangements, for a combined total of SDR 36.8 million. In addition, the Board approved Kenya's request to reduce access under its PRGF arrangement by SDR 75 million, in light of its improved external position. As of April 30, 2007, the reform programs of 29 member countries were supported by PRGF arrangements. Total concessional loans outstanding amounted to SDR 3.9 billion (Figure 3.2). To date, no country has requested assistance under the ESF.

37 *"The Role of Fund Support in Crisis Prevention" (March 23, 2006) can be found on the IMF's Web site,* www.imf.org.

38 *The summing up of the Board's discussion is contained in PIN 06/104, which can be found on the CD-ROM and on the IMF's Web site, at* www.imf.org/external/np/sec/pn/2006/pn06104.htm. *A fact sheet about the Contingent Credit Lines can be found at* www.imf.org/external/np/exr/facts/ccl.htm. *The IMF introduced the CCL in 1999 as part of its response to the rapid spread of turmoil through global financial markets during the Asian crisis of 1997–98. The instrument was intended to provide a precautionary line of defense for members that had sound policies and were not at risk of an external payments crisis of their own making, but that were vulnerable to contagion effects from capital account crises in other countries. Despite changes intended to make the CCL more attractive to members, it was never used, and the Board decided in 2003 to allow it to expire.*

39 *The staff paper, "Further Consideration of a New Liquidity Instrument for Market Access Countries—Design Issues," February 13, 2007, can be found on the IMF's Web site, at* www.imf.org/external/pp/longres.aspx?id=4044. *The summing up of the Board's discussion, PIN 07/40, can be found on the CD-ROM as well as on the Fund's Web site, at* www.imf.org/external/np/sec/pn/2007/pn0740.htm.

Table 3.2 PRGF arrangements approved in FY2007

(In millions of SDRs)

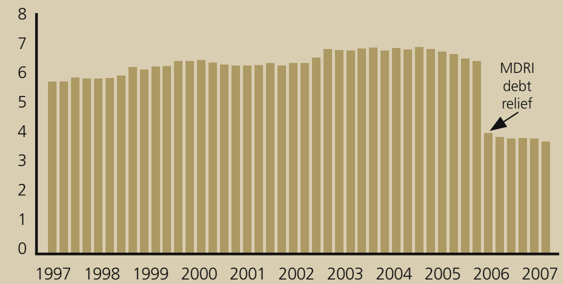
Member	Effective date	Amount approved[1]
New arrangements		
Afghanistan	June 26, 2006	81.0
Burkina Faso	April 23, 2007	6.0
Central African Rep.	December 22, 2006	36.2
Gambia, The	February 21, 2007	14.0
Haiti	November 20, 2006	73.7
Madagascar	July 21, 2006	55.0
Mauritania	December 18, 2006	16.1
Moldova	May 5, 2006	80.1
Rwanda	June 12, 2006	8.0
Sierra Leone	May 10, 2006	31.1
Subtotal		**401.2**
Augmentations/reductions		
Burkina Faso	September 8, 2006	6.0
Moldova	December 15, 2006	30.8
Kenya	April 11, 2007	(75.0)
Subtotal		**(38.2)**
Total		**363.0**

Source: IMF Finance Department.

1 For augmentations/reductions, only the amount of the increase/decrease is shown.

Figure 3.2 Concessional loans outstanding, FY1997–FY2007

(In billions of SDRs)



Source: IMF Finance Department.

Debt relief

Debt relief efforts under the enhanced HIPC Initiative and the MDRI continued during FY2007. A sunset clause was introduced at the start of the HIPC Initiative in 1996, restricting eligibility to countries that had embarked on programs supported by the IMF or the International Development Association (IDA)[40] within a two-year period to prevent the Initiative from becoming permanent, minimize potential moral hazard arising from excessive borrowing in anticipation of debt relief, and encourage early adoption of reforms. Following numerous extensions over the years, at a meeting in September 2006 the Executive Boards of the IMF and the World Bank acknowledged that letting the sunset clause take effect at end-2006 without any modification could leave several countries with debt burdens in excess of the Initiative's thresholds and no further possibility of benefiting from this comprehensive framework. Accordingly, agreement was reached to let the sunset clause take effect while grandfathering all countries assessed to have met the income and indebtedness criteria based on end-2004 data, including countries that might be assessed to have met these criteria at some point in the future.

Executive Directors called on the staff to conduct a stocktaking exercise in a few years' time to review the options for the remaining duration of the HIPC Initiative. They also urged staff to continue working with country authorities to develop and implement reform strategies and to assist these countries in qualifying for HIPC Initiative assistance promptly. At the same time, they encouraged the remaining countries to make every effort to establish a track record of policy performance and implement satisfactorily their poverty reduction strategies so that they can begin receiving debt relief.[41]

As of April 30, 2007, 30 countries had reached the decision point under the enhanced HIPC Initiative; of these, 22 had reached their completion points.[42] The IMF has committed SDR 1.9 billion under the HIPC Initiative and disbursed SDR 1.7 billion. During FY2007, one member (Haiti) reached its decision point, three others (Malawi, Sierra Leone, and São Tomé and Príncipe) reached their completion points, and Afghanistan was added to the list of countries eligible for assistance under the HIPC Initiative.

40 IDA is the World Bank agency that provides interest-free loans and grants to the poorest member countries.

41 For the summing up of the Board's discussion, see "IMF Executive Board Discusses Issues Related to the Sunset Clause of the Initiative for Heavily Indebted Poor Countries," PIN 06/107, on the CD-ROM or at www.imf.org/external/np/sec/pn/2006/pn06107.htm.

42 To qualify for HIPC assistance, a country must pursue strong economic policies supported by the IMF and the World Bank. After establishing a track record of good performance and developing a PRSP or an interim PRSP, the country is said to have reached its decision point, at which time the IMF and the World Bank formally decide on the country's eligibility and the international community commits itself to reducing the country's debt to a sustainable level. The country must then continue its good track record with the support of the international community, implementing key policy reforms, maintaining macroeconomic stability, and adopting and implementing a PRSP. Paris Club and other bilateral and commercial creditors reschedule obligations coming due. A country reaches its completion point once it has met the objectives set at the decision point. It then receives the balance of the debt relief committed.

Box 3.2 Tracking progress toward the Millennium Development Goals

The IMF and the World Bank track the progress made by low-income countries toward the achievement of the Millennium Development Goals (MDGs), jointly publishing their findings annually in the *Global Monitoring Report* (GMR). The fourth GMR, issued in April 2007, found that progress on the first goal—halving poverty by 2015—was on track in all developing regions except sub-Saharan Africa, but that efforts to attain the goals of reducing child mortality and disease and achieving environmental sustainability were falling short. It called for greater attention to gender equality—not only because of equity considerations but also because empowering women is essential to economic well-being and the advancement of the other MDGs—and to fragile states, which account for 27 percent of the developing world's extreme poor (those living on less than $1 a day).[1] Fragile states—low-income countries and territories deemed to have especially weak institutions and governance that undermine economic performance and the delivery of basic social services—are, in general, the least likely to achieve the MDGs. Many are emerging from conflict.

A substantial increase in aid will be needed if developing countries are to accelerate their efforts to reach the MDGs. However, actual commitments of aid in 2005–06 as registered by the OECD-DAC (Organization for Economic Cooperation and Development–Development Assistance Committee)—excluding exceptional debt relief transactions—have declined, and projections through 2008 have aid volumes falling well short of the pledges made by the international community at the International Conference on Financing for Development that took place in Monterrey, Mexico, in 2002, and at the Group of 8's Gleneagles summit in 2005. The IMF continues to urge bilateral donors to increase aid levels and make aid more predictable. The Fund is also providing advice and technical assistance in its areas of expertise to aid recipients to ensure that they can use increased aid effectively without undermining macroeconomic stability, crowding out private investment, or falling back into situations of unsustainable external indebtedness.

The IMF works closely with the World Bank on many issues related to low-income countries in addition to the GMR, including the PRSP process, debt relief under the HIPC Initiative and the MDRI, the Debt Sustainability Framework, and the Financial Sector Assessment Program (the FSAP is described in Chapter 2). An External Committee carried out a study on Bank-Fund collaboration, which is discussed in Chapter 5, during FY2007.

1 The Global Monitoring Report: Confronting the Challenges of Gender Equality and Fragile States*can be found on the IMF's Web site, at* www.imf.org/external/pubs/cat/longres.cfm?sk=20364.0.

The MDRI was launched in early 2006 to further reduce the debts of qualifying low-income countries and provide them with additional resources to help meet the MDGs. Proposed by the Group of 8 countries, the MDRI is a different mechanism from the HIPC Initiative but linked to it operationally. Under the MDRI, the IMF, IDA, the African Development Fund, and the Inter-American Development Bank provide 100 percent debt relief on eligible claims of countries reaching the completion point under the enhanced HIPC Initiative. In addition, the IMF provides MDRI debt relief to all its members with yearly per capita incomes at or below $380 (including two non-HIPCs, Cambodia and Tajikistan).[43]

As of April 30, 2007, the IMF had delivered MDRI debt relief totaling SDR 2.7 billion to 24 countries. The debt relief was financed by a combination of resources from undisbursed

43 For more information on the MDRI, see PIN 05/164, at www.imf.org/external/np/sec/pn/2005/pn05164.htm.

Box 3.3 Trade liberalization and low-income countries

In August 2006, the Executive Board discussed the "Doha Development Agenda and Aid for Trade," a paper jointly prepared by the staffs of the IMF and the World Bank.[1] Executive Directors stressed that work on Aid for Trade should proceed regardless of the status of the Doha Round. Although Aid for Trade cannot substitute for an ambitious outcome to the Doha Round, by helping developing countries address infrastructural and other supply constraints, it may enable them to take full advantage of trade opportunities arising from global market opening. The IMF should continue with selective interventions within its mandate and core areas of competence, including the macroeconomic implications of changes in trade policies and the global trade environment, and advice on tax and customs reform.

The Board took note of the proposals of the WTO Task Forces on an Enhanced Integrated Framework for Trade-Related Technical Assistance (IF) and on Aid for Trade. At present, trade-related priorities in many of the least-developed countries remain disconnected from the PRSP process. Against this background, Executive Directors observed that implementation of the recommendations of the IF Task Force could allow the IF to play a more effective role in helping to identify aid-for-trade needs and coordinating trade-related technical assistance. They welcomed the recommendations for strengthened capacity in IF beneficiary countries and improved IF governance, and recognized donor commitments for the financing of this effort.[2]

Although the benefits of trade liberalization outweigh the costs overall, certain low-income countries may be hurt in the short run by trade liberalization measures that expose their exports to greater competition, reduce their revenues as tariffs are lowered, or raise the cost of food imports as agricultural subsidies are abolished. In 2004, the IMF introduced the Trade Integration Mechanism (TIM), a vehicle that allows countries to increase their access to IMF resources under an existing arrangement or a new arrangement within one of the Fund's facilities if necessary to cope with the erosion of trade preferences and the effect of other countries' trade liberalization on their balance of payments. In FY2007, the Executive Board approved the activation of the TIM for Madagascar, in light of the possible impact on the country's textile exports of the expiration of textile quotas in 2005 as called for by the WTO's Agreement on Textiles and Clothing and the implementation of the U.S. African Growth and Opportunities Act in 2007. With the activation of the TIM, Madagascar became eligible for an augmentation of access to IMF resources under its PRGF arrangement. It is the third IMF member for which the TIM has been activated.

1 *The paper is available on the IMF's Web site, at* www.imf.org/external/pp/longres.aspx?id=3886; *PIN 06/105, which contains the summing up of the Board's discussion, can be found on the CD-ROM or at* www.imf.org/external/np/sec/pn/2006/pn06105.htm.

2 *The recommendations include the establishment of a new executive secretariat in the WTO Secretariat, measures to strengthen capacity in the least-developed countries, a funding target of $400 million over an initial five-year period, and a monitoring and evaluation framework.*

HIPC accounts (SDR 0.4 billion), IMF resources (SDR 1.2 billion), and bilateral contributions (SDR 1.1 billion). During FY2007, four members (Malawi, Mauritania, Sierra Leone, and São Tomé and Príncipe) received debt relief totaling SDR 189.2 million under the MDRI.[44]

Debt Sustainability Framework

The primary aim of the DSF is to help guide the borrowing decisions of low-income countries, balancing their need for funds against their ability to service debt. The Executive Board had a second discussion in FY2007 about how the DSF, which was

44 CD-Table 3.3 and CD-Table 3.4 on the CD-ROM list the countries covered by the MDRI and describe the implementation of the MDRI.

endorsed by the Boards of the IMF and the World Bank in April 2005, could be used to help low-income countries that have received debt relief avoid reaccumulating excessive debt.[45] The November 2006 discussion, which was based on a paper prepared jointly by the staffs of the IMF and the World Bank, focused on how best to integrate into the DSF the policy challenges arising from the perceived increase in borrowing space created by debt relief in some low-income countries, the emergence of new creditors, and the rising weight of domestic debt. These developments, while welcome, create new risks that need to be addressed as countries make progress toward implementing prudent debt-management policies. The Board therefore called for improvements to the rigor and quality of debt sustainability analyses.

Executive Directors reiterated that concessional flows remain the most appropriate source of external finance for low-income countries and called for continued efforts by the international community to improve the availability and predictability of such financing. However, they recognized that consideration should be given, on a case-by-case basis, to nonconcessional finance, depending on its impact on debt sustainability, on the overall strength of a borrowing country's policies and institutions, and on the quality of both the investment to be financed and the overall public expenditure program.

Executive Directors underscored that the effectiveness of the DSF ultimately depends on its broader use by debtors and creditors and stressed the need for further outreach to official creditors. They also stressed the importance of timely, high-quality data on borrowing and lending operations and encouraged IMF staff, working with Bank staff, to disseminate more broadly and effectively the results of debt sustainability analyses.[46] The Board welcomed the creation of a dedicated Web page on the IMF's Web site where debt sustainability analyses can be easily located and supported the establishment of a similar Web page on concessionality.[47] The IMF and the World Bank have stepped up their outreach on the DSF, including to non-OECD creditors, to foster responsible lending practices, and they stand ready to help design principles in this area. They are also increasing efforts to provide borrowing countries with training and technical assistance to strengthen their debt-management capacities.

Agricultural worker in Tajikistan

Policy Support Instrument

In recent years, several low-income countries have made significant progress toward economic stability and no longer require IMF financial assistance. However, regardless of whether they seek the Fund's financial support, they may still seek IMF monitoring and support of, and advice and counsel on, their economic policies. Approved by the Executive Board in FY2006, PSIs are designed to address the needs of these members by providing policy support and "signaling."[48] Signaling refers to the information Fund activities can indirectly provide about countries' performance and prospects. Such information can be used to inform the decisions of outsiders, including private creditors, official donors and creditors, and the public at large. In low-income countries, such signals have been sent mainly in the context of the PRGF and the related PRSP process. PSIs mirror the design and achieve many of the purposes of the PRGF, and like PRGF arrangements and debt relief, are based on development of a PRSP. They are also voluntary—members that want PSIs must request

45 *The first discussion took place in April 2006; see PIN 06/61, at* www.imf.org/external/np/sec/pn/2006/pn0661.htm.

46 *For the summing up of the Board's discussion, see PIN 06/136, "IMF Executive Board Discusses the Application of the Debt Sustainability Framework for Low-Income Countries Post Debt Relief" on the CD-ROM or at* www.imf.org/external/np/sec/pn/2006/pn06136.htm. *The staff report can be found on the IMF's Web site, at* www.imf.org/external/pp/longres.aspx?id=3959; *a staff guidance note on the application of the DSF is also posted on the IMF's Web site, at* www.imf.org/external/np/pp/2007/eng/041607.pdf.

47 *See* www.imf.org/external/pubs/ft/dsa/lic.aspx *for debt sustainability analyses included in country reports. The Web page on the IMF's concessionality was launched in January 2007; see* www.imf.org/external/np/pdr/conc/index.htm.

48 *See PIN 05/145 at* www.imf.org/external/np/sec/pn/2005/pn05145.htm *for the summing up of the Board discussion at which the PSI was approved.*

them—and thus demonstrate strong country ownership of policy programs, and programs are expected to meet the same high standards as programs supported by Fund financial assistance. In the event of a shock, an on-track PSI could provide the basis for rapid access to PRGF resources through the ESF. The publication of PSI documents, like that of PRGF documents, is voluntary but presumed.

The IMF provides emergency financial assistance to emerging market economies and low-income countries recovering from conflicts or natural disasters.

In addition to promoting a close policy dialogue between the IMF and its low-income members, PSIs provide more frequent Fund assessments of members' economic and financial policies than is possible under the Article IV consultation process: while Article IV consultations usually take place yearly, the Board reviews performance under PSIs semiannually. Members with PSIs are expected to provide timely and accurate data to the Fund to ensure the integrity of these assessments.

In the past two years, the Board has approved PSIs for four countries: Nigeria and Uganda in FY2006, and Cape Verde and Tanzania in FY2007.[49] In FY2007, the Board reviewed Uganda's 16-month PSI and approved a new, 3-year PSI at Uganda's request.

Emergency Assistance

The IMF provides emergency financial assistance to both emerging market economies and low-income countries recovering from conflicts (Emergency Post-Conflict Assistance, or EPCA) or natural disasters (Emergency Natural Disaster Assistance, or ENDA). The interest charged on Emergency Assistance provided to PRGF-eligible members is subsidized subject to the availability of subsidy resources contributed by member countries; the subsidized rate is 0.5 percent a year.

During FY2007, the Executive Board approved Emergency Assistance of SDR 50.8 million for Lebanon under EPCA, and the Central African Republic and Haiti repaid their EPCA loans, totaling SDR 33 million, earlier than scheduled. As of April 30, 2007, two countries, Iraq and Lebanon, had outstanding EPCA credit, which amounted to SDR 347.9 million. No new ENDA loans were made during FY2007. During FY2007, Malawi repaid ENDA loans totaling SDR 8.7 million. Three countries—Grenada, Maldives, and Sri Lanka—had outstanding ENDA credit, for a total of SDR 111.5 million, at end-April 2007.

Review of the IMF's Role and Instruments

In FY2007, the Executive Board reviewed the IMF's advice on the use of aid in sub-Saharan Africa, based on an IEO evaluation; considered the findings and value of ex post assessments; and compared the performance of countries under precautionary arrangements with that of countries that had arrangements on which they drew financial assistance. The Board also requested additional policy papers to define more clearly the IMF's role in low-income countries.

IMF and aid to sub-Saharan Africa

In March 2007, the Executive Board discussed the IEO evaluation of the IMF and aid to sub-Saharan Africa.[50] The IEO report confirmed the steady improvement in the region's macroeconomic performance during 1999–2005 and attributed this improvement in part to the advice and actions of the IMF, including on debt relief, while also recognizing the contribution of the authorities' own efforts and exogenous factors. Nevertheless, the report

49 *For details, see Press Releases 06/172, "IMF Executive Board Approves a Three-Year Policy Support Instrument for Cape Verde," and 07/13, "IMF Executive Board Completes the First Review Under the Policy Support Instrument for Cape Verde," at* www.imf.org/external/np/sec/pr/2006/pr06172.htm *and* www.imf.org/external/np/sec/pr/2007/pr0713.htm, *respectively; Press Releases 05/229, "IMF Executive Board Approves a Two-Year Policy Support Instrument for Nigeria," and 06/293, "IMF Executive Board Completes the Second Review Under the Policy Support Instrument for Nigeria," at* www.imf.org/external/np/sec/pr/2005/pr05229.htm *and* www.imf.org/external/np/sec/pr/2006/pr06293.htm, *respectively; Press Release 07/26, "IMF Executive Board Completes Sixth Review Under Tanzania's PRGF Arrangement and Approves a Three-Year Policy Support Instrument," at* www.imf.org/external/np/sec/pr/2007/pr0726.htm; *and Press Releases 06/14, "IMF Executive Board Completes Final Review of Uganda's PRGF Arrangement and Approves 16-Month Policy Support Instrument," and 06/281, "IMF Executive Board Completes the First Review Under the Policy Support Instrument for Uganda and Approves a New Three-Year Policy Support Instrument," at* www.imf.org/external/np/sec/pr/2006/pr0614.htm *and* www.imf.org/external/np/sec/pr/2006/pr06281.htm, *respectively.*

50 *The IEO's report and press release, as well as the summing up of the IMF Board's discussion, can be found at* www.ieo-imf.org/eval/complete/eval_03122007.html.

Post-conflict reconstruction in Lebanon

identified areas where further improvements were needed, including the IMF's role in poverty reduction efforts, the mobilization of aid, the preparation of alternative scenarios for reaching the MDGs, and the application of poverty and social impact analysis. The IEO found that IMF staff did not receive clear directives on work in these areas because of differences in the views of Executive Directors on the IMF's role and policies in low-income countries, and that management and the Board should have done more to resolve these differences. The report also found a disconnect between the IMF's external communications on aid and poverty reduction and its practice in low-income countries.

The IEO made the following recommendations: (1) the Executive Board should clarify IMF policies on macroeconomic performance thresholds for the accommodation of additional aid, the mobilization of aid, alternative scenarios, poverty and social impact analysis, and pro-poor and pro-growth budget frameworks; (2) IMF management should establish transparent mechanisms for monitoring and evaluating the implementation of the clarified policy guidance, including with respect to collaboration with the World Bank, and ensure that institutional communications are consistent with Fund policies and operations; and (3) management should clarify its expectations of, and the resources available to, the IMF's resident representatives and mission chiefs with respect to their interactions with local donor groups and civil society.

In their discussion of the IEO's report, Executive Directors were encouraged by the improvements in sub-Saharan Africa's macroeconomic performance. They noted that the HIPC Initiative and the MDRI had greatly reduced debt-related vulnerabilities and the costs of debt servicing. Executive Directors also noted the improvements in the IMF's assistance to low-income countries. They considered that the IMF's engagement in low-income countries should remain focused on its core mandate and that the IMF should not play a coordinating role in aid mobilization. They also confirmed that distributional policies lie outside the IMF's core mandate and emphasized the importance of improving IMF collaboration with development partners, in particular the World Bank, to take these issues into account when helping countries formulate their macroeconomic policies. Many Executive Directors thought staff should be prepared to design alternative scenarios related to the scaling-up of aid, but most thought that normative advice would fall outside the IMF's mandate: they considered that the IMF's role should be limited to assessing the consistency of additional aid flows with macroeconomic stability and the absorption capacity of the country. The Board supported the report's recommendation on the need for further clarification of IMF policy and asked staff to come back with specific proposals in this area. Early in FY2008, Fund management submitted its plan for implementing Board-endorsed recommendations to the Board.

Ex post assessments

Ex post assessments (EPAs) provide the IMF with an opportunity to step back from ongoing longer-term program engagement with a member country so that it can take a fresh look at its overall strategic approach and draw lessons for future programs. In May 2006, the Executive Board discussed the IMF staff's "Review of Ex Post Assessments and Issues Relating to the Policy on Longer-Term Program Engagement."[51] Through May 15, 2006, 57 members had been identified as having longer-term program engagement, of which more than 80 percent were low-income countries, and 42 EPAs had been completed. The IMF introduced EPAs in 2003 in response to the IEO's report on prolonged use of Fund resources because of concerns that, in some cases, longer-term program engagement might indicate inadequate progress in dealing with members' economic problems and a lack of effectiveness of IMF-supported programs. There were also concerns that longer-term program engagement might hinder the development of domestic institutions, undermine the Fund's credibility, and decrease the resources available to other members in need of support.

In their May 2006 discussion, Executive Directors reviewed the findings of 32 EPA reports completed by end-August 2005.[52] In most cases, EPAs found that the design of policies in IMF-supported programs had been consistent with the multiple macroeconomic and structural challenges faced by members with longer-term program engagement, and that IMF involvement had not undermined members' institutional development. The Board noted, however, that several EPAs had been critical of the design of structural reforms, in terms of both the scope and the number of structural conditions, and that efforts to streamline conditionality should continue.

The Board considered that, by and large, EPAs have served their purpose and remain an important institutional mechanism for distilling lessons and enhancing the learning culture of the IMF. However, their value could be enhanced by greater selectivity and focus on a few critical issues. Executive Directors suggested that systematic discussions in EPAs of the reasons for program success or failure and of potential exit strategies would provide further useful lessons and generally agreed that, the IMF's budget situation permitting, the staff should expand efforts to reach out and consult with donors, outside experts, and country authorities, while safeguarding the confidentiality of information.

Precautionary arrangements

Also in May 2006, the Board discussed a study by IMF staff comparing precautionary programs with lending programs on which borrowing countries intend to draw. The study was undertaken at the Board's request to determine whether there were systematic differences in terms of program policies, conditionality, or macroeconomic outcomes, and, if so, whether such differences were attributable to the nature of the program or to the circumstances that had led the member to seek the IMF's support. Executive Directors concurred that drawing programs were more likely to be requested by members with weaker macroeconomic performances, whereas precautionary programs tended to be requested by members that had stronger macroeconomic fundamentals but faced uncertainties.[53] It was also recognized that members used precautionary programs to signal policies to markets. The Board noted that, in the first program year, output growth was significantly higher, and inflation significantly lower, in members with precautionary programs than in those with drawing programs. However, these differences could be explained largely by the differences in initial conditions. Executive Directors welcomed the analysis of market reactions, as reflected in interest rate spreads, to IMF-supported programs. Spreads did not widen when members sought precautionary programs, suggesting that markets did not attach a stigma to such programs.

Executive Directors expressed a variety of views on the role of precautionary arrangements in supporting a successful exit for members from IMF-supported programs. They considered that all IMF-supported programs should aim to achieve an exit from IMF financing. Overall, Executive Directors agreed that precautionary programs are a most useful instrument in the IMF's toolkit, lending the IMF's credibility in support of the authorities' policies and enhancing policy discipline. Many Executive Directors also considered that these programs send a well-calibrated signal to markets of the authorities' commitment. Comparisons of policy objectives and conditionality between precautionary and non-precautionary programs suggested to most Executive Directors that IMF policies are being applied consistently.

51 *The paper can be found on the IMF's Web site, at* www.imf.org/external/np/pp/eng/2006/032006R.pdf. *The summing up of the Board discussion can be found in PIN 06/96, on the CD-ROM, as well as on the IMF's Web site,* www.imf.org/external/np/sec/pn/2006/pn0696.htm.

52 *These EPAs were for the following countries: Albania, Armenia, Azerbaijan, Benin, Bolivia, Bulgaria, Cambodia, Cameroon, Chad, Ethiopia, The Gambia, Georgia, Guinea, Guinea-Bissau, Honduras, Kazakhstan, the Kyrgyz Republic, Lesotho, the former Yugoslav Republic of Macedonia, Madagascar, Malawi, Mali, Moldova, Mozambique, Niger, Peru, Romania, Sierra Leone, Uganda, Uruguay, Vietnam, Zambia.*

53 *PIN 06/94, which contains the full summing up of the Board discussion, can be found on the CD-ROM and on the IMF's Web site, at* www.imf.org/external/np/sec/pn/2006/pn0694.htm.

Chapter 4

Chapter 4 Capacity building: technical assistance and training

The technical assistance and training offered by the IMF at the request of member countries are intended to help them fulfill the commitments they make when they join the IMF—to pursue policies that foster financial and macroeconomic stability, sustainable economic growth, and orderly exchange rate arrangements, and to provide the IMF with timely, accurate, and high-quality data about their economies. Equally important, technical assistance and training are also vehicles for helping member countries implement the recommendations that come out of the IMF's Article IV consultations (see Chapter 2). Hence, aligning and integrating capacity building with surveillance and program work have become key objectives of the IMF's Executive Board, which regularly reviews Fund technical assistance and training.

The IMF offers technical assistance and training mainly in its core areas of expertise, including macroeconomic policy, tax and revenue administration, public expenditure management, monetary policy, exchange systems, financial sector reforms, and macroeconomic and financial statistics. In recent years, member countries have also increasingly requested assistance in addressing issues related to monitoring offshore financial centers, preventing money laundering and the financing of terrorism, strengthening public investment, managing fiscal risks from public-private partnerships, adopting international standards and codes for data and financial and fiscal management, correcting weaknesses identified under the joint IMF–World Bank Financial Sector Assessment Program, and carrying out debt sustainability analyses.

The amount of technical assistance and training delivered directly to member countries by the IMF has increased over the past five years with the expansion of the regional technical assistance and training centers. Taking management and administration into account, technical assistance now represents about 24 percent of the IMF's operating budget. Still, demand for technical assistance and training exceeds the IMF's ability to supply it, especially in light of constraints stemming from growing pressures on the IMF's finances. Priority is therefore given to initiatives that support the IMF's core objectives.

IMF technical assistance is delivered mainly by the Monetary and Capital Markets Department (MCM), Fiscal Affairs Department (FAD), Statistics Department (STA), and Legal Department (LEG). Overall institutional policy on, and coordination of, technical assistance are the responsibility of the Committee on Capacity Building, assisted by the Office of Technical Assistance Management (OTM), in consultation with other IMF departments. Following up on the IMF's Medium-Term Strategy, the Committee on Capacity Building is charged with ensuring that the IMF's initiatives in this area respond to country needs, are coordinated with other providers, and are guided by appropriate policies, while OTM is responsible for raising and managing external financing for technical assistance activities and policy support. Training activities are handled primarily by the IMF Institute, which conducts seminars, workshops, and other training events for country officials, often in collaboration with other IMF departments.

Recognizing the critical capacity-building needs of developing countries, the IMF in FY2007 opened a regional technical assistance center (RTAC) in Gabon to support countries in Central Africa—the third such center in Africa and the sixth worldwide (Box 4.1)—as well as a seventh Regional Training Center (RTC) program, in India.

Technical Assistance

While the IMF may help identify areas of need, it is the member country that decides to request technical assistance. Most technical assistance is provided free of charge. Whether technical assistance is delivered through missions from headquarters, short-term expert assignments, long-term resident advisors, or regional centers, the recipient country is always fully involved in selecting, implementing, monitoring, and evaluating the assistance it receives. This collaborative approach strengthens country ownership of reforms.

Regional training center for Latin America

Box 4.1 Regional Technical Assistance Centers

The RTACs are collaborative ventures between the IMF, the recipient countries, and bilateral and multilateral donors. Financial support for them comes from the donors, and, in many instances, the recipient countries themselves, as well as from the IMF. Host governments frequently provide in-kind contributions.

The RTACs were originally conceived to provide technical assistance to small island economies, because individual assistance providers, including the IMF, were hard pressed to meet these countries' requests. The Pacific RTAC, the first, was established in 1993 to serve 15 island nations. Building on its success, other RTACs soon followed, and today there are six RTACs worldwide.

The Caribbean RTAC (CARTAC), established in 2003, serves 20 countries. The East AFRITAC, established in Dar-es-Salaam, Tanzania, in 2002, and the West AFRITAC, established in Bamako, Mali, in 2003, together serve 17 countries. The new Central AFRITAC, which opened in Libreville, Gabon, in FY2007, serves the six countries of the Central African Economic and Monetary Community (CEMAC)—Cameroon, Chad, the Central African Republic, the Republic of Congo, Equatorial Guinea, and Gabon—as well as Burundi and the Democratic Republic of the Congo. The Middle East RTAC, established in 2004, serves 10 countries and territories in the Middle East, primarily with technical assistance related to rebuilding their economies as they emerge from conflict.

The growing focus on the regional dimensions of IMF technical assistance is in line with the expansion of the IMF's regional surveillance activities as trade and financial integration—and the possibility of spillovers—increase. In addition, the RTACs facilitate coordination with other technical assistance providers, encourage the sharing of regional experiences, and foster the development of regional networks of experts. In its review of the RTACs in FY2006, the IMF's Executive Board concluded that they were a useful addition to the Fund's technical assistance program and that their presence in the field had notable advantages—in particular, the strengthening of countries' ownership of their technical assistance programs and the provision of rapid and flexible technical assistance.

The volume of technical assistance, measured in person-years, delivered through the RTACs has risen every year since FY2002, both in absolute terms and as a proportion of total IMF technical assistance (see CD-Table 4.1, on the CD-ROM). Since the establishment of the East and West AFRITACs, the annual volume of IMF technical assistance and training provided in sub-Saharan Africa has increased by almost 30 percent.

The RTACs are staffed by teams of resident experts, supplemented by short-term specialists, who provide capacity-building assistance through advisory services and training in the core areas of the IMF's expertise, including debt management, financial sector policy, revenue administration, public financial management, and macroeconomic statistics. The Steering Committees that govern the RTACs set the centers' strategic direction and review rolling work plans, promoting strong country ownership of the centers themselves and the technical assistance delivered through them. CARTAC is a United Nations Development Program project in which the IMF is a signatory; the others are IMF operations for which the IMF has sought funding from donors.

Details on the countries served by the RTACs, the donors for the different RTACs, and the fields of expertise of resident advisors can be found on the CD-ROM, in CD-Table 4.2.

Ninety percent of IMF technical assistance is provided to low- and lower-middle-income countries (Table 4.1), to help them build the institutions and capacity needed to implement growth-enhancing policies. Technical assistance delivery trends in FY2007 are summarized in Table 4.2.

Direct financing for technical assistance delivery, supervision, and administrative and other costs comes from the Fund's administrative budget. Bilateral and multilateral donors have provided generous financial assistance as well, covering about 26 percent of the direct cost. This cooperation with external donors both leverages the internal resources available for technical assistance and heads off duplication of effort.

Table 4.1 Technical assistance by country income group, FY2007

(Field delivery in person-years)[1]

Country income group	Total person-years	Percent of total
Low-income	64.2	33.4
Lower-middle-income	114.8	59.8
Upper-middle-income[2]	8.8	4.6
High-income[2]	4.2	2.2
Total	**192.1**	**100.0**

1 An effective person-year of technical assistance is 260 days.

2 Pertains mostly to regional seminars and workshops delivered in upper-middle- and high-income countries but attended by officials from low- and lower-middle-income countries.

Table 4.2 IMF technical assistance resources and delivery, FY2005–07

(In effective person-years)[1]

	FY2005	FY2006	FY2007
IMF administrative budget	**283.4**	**337.6**	**325.1**
External resources	**97.1**	**87.3**	**113.3**
Total resources	**380.6**	**424.9**	**438.4**
Regional delivery	**301.4**	**288.4**	**308.3**
Africa	86.9	82.4	90.4
Asia and Pacific	68.2	58.5	62.7
Europe	34.5	37.1	34.6
Middle East and Central Asia	45.1	61.0	54.2
Western Hemisphere	32.7	37.5	48.2
Regional and interregional	33.9	11.9	18.2
Management and administration[2]	**79.2**	**136.5**	**130.1**
Total delivery	**380.6**	**424.9**	**438.4**
Total delivery by department	**380.6**	**424.9**	**438.4**
Fiscal Affairs Department	99.5	100.2	116.9
Monetary and Capital Markets Department[3]	127.0	125.7	117.0
Statistics Department	53.1	54.3	56.3
IMF Institute	57.0	76.4	78.4
Legal Department	23.5	20.0	26.0
Other departments[4]	20.4	48.3	43.8

Source: IMF Office of Technical Assistance Management.

Note: Some data have been adjusted retroactively to reflect new definitions.

1 An effective person-year of technical assistance is 260 days.

2 Indirect technical assistance, including technical assistance policy, management, evaluation, and other related activities.

3 In FY2005 and FY2006, technical assistance was delivered by the Monetary and Financial Systems Department, which merged with the International Capital Markets Department to become the Monetary and Capital Markets Department in FY2007.

4 Includes the Policy Development and Review Department, the Technology and General Services Department, the Office of Technical Assistance Management, the Finance Department, the Human Resources Department, and all area departments.

Following on the Board's endorsement in FY2006 of proposals made by the Task Force on Technical Assistance on how to implement the recommendations in the Independent Evaluation Office's FY2005 report on Fund technical assistance,[54] the IMF has developed a strategic medium-term approach that closely integrates and prioritizes country needs and technical assistance resources with the IMF's budget process. In addition, the IMF's technical assistance strategy is being increasingly viewed from a regional perspective, in recognition of the synergies and benefits that a regional approach can bring to technical assistance. Regional strategies also help the IMF prioritize and shift its resources between neighboring countries, in response to developing needs and changing circumstances.

As called for by the Executive Board, the IMF will continue to make improvements to its technical assistance program in the year ahead, including further strengthening the monitoring and evaluation of technical assistance to ensure its effectiveness and efficiency (CD-Table 4.3). Other aspects of technical assistance management and governance emphasized by the Board are also being studied, including improving cost information on technical assistance activities, reinforcing relationships with donors to the IMF's technical assistance program (Table 4.3), and enlisting support from new donors.

The IMF's Monetary and Capital Markets Department (MCM) provides technical assistance related to the implementation of monetary and foreign exchange policies and other aspects of central banking, financial sector oversight and regulation, the development of capital and other financial markets, and public sector debt and asset management. This assistance generally involves advising central banks and financial supervisory agencies on strengthening institutions and policies and improving consistency with international standards, codes, and good practices, and is typically delivered by staff from IMF headquarters and short-term experts, who in many cases are financed with the assistance of donors. MCM's advice is also delivered by long-term experts located in the IMF's regional technical assistance centers, and may take the form of regional seminars and hands-on workshops. Examples of MCM's technical assistance activities in FY2007 include

Table 4.3 Donors to the IMF's technical assistance program

	Donors
Individual donors[1]	Australia, Belgium, Canada, Denmark, France, Italy, Japan, Luxembourg, the Netherlands, Norway, Spain, Sweden, Switzerland, United Kingdom
Multidonor pooled arrangements	
Africa Technical Assistance Centers (East and West)	African Development Bank, Canada, China, Denmark, Finland, France, Germany, Italy, Japan, Luxembourg, the Netherlands, Norway, Russia, Sweden, Switzerland, United Kingdom
Caribbean Regional Technical Assistance Center	Canada, Ireland, United Kingdom, United States, European Union, Inter-American Development Bank, UNDP, World Bank
Central Africa Technical Assistance Center	African Development Bank, Burundi, Cameroon, Central African Republic, Chad, Democratic Republic of the Congo, Republic of Congo, Equatorial Guinea, France, Gabon, Germany
Financial Sector Reform and Strengthening Initiative	Canada, the Netherlands, Switzerland, United Kingdom, World Bank
Iraq Technical Assistance	Australia, Canada, India, Italy, Sweden, United Kingdom
Middle East Technical Assistance Center	Egypt, European Union, European Investment Bank, France, Japan, Jordan, Kuwait, Lebanon, Libya, Oman, Qatar, Saudi Arabia, Sudan, Syrian Arab Republic, United Arab Emirates, Republic of Yemen
Pacific Financial Technical Assistance Centre	Asian Development Bank, Australia, Japan, Korea, New Zealand

1 Some donors contribute both individually and through multidonor pooled agreements.

54 *The Task Force's report is available at* www.imf.org/external/np/pp/eng/2005/071205.htm; *the summary of the Board discussion can be found at* www.imf.org/external/np/sec/pn/2005/pn05114.htm.

supporting Nigeria's financial sector reform program and helping the Philippines' central bank strengthen its ability to identify the risks associated with complex domestic conglomerates, based on Financial Sector Assessment Programs in both countries; and advising Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and Panama on improving public debt management and carrying out a diagnostic study of Central American markets for private equity, debt, and asset-backed securities.[55]

The Fiscal Affairs Department (FAD) provides a range of technical assistance and training to help countries strengthen their fiscal policies and institutions, enhance implementation capacity, and support IMF surveillance. For example, during FY2007, FAD staff provided advice on modernizing tax and customs administration in China, Mexico, and Turkey; continued advising the Central American countries on improving the coordination of their tax policies and tax administration and preparing the legislative framework for a regional customs union; assisted a number of post-conflict countries, including Afghanistan, Lebanon, Liberia, and Sudan, seeking to rebuild their revenue-administration capacity; conducted, with the support of the East AFRITAC and private sector involvement, a seminar on improving taxpayer services and appeals as a means of increasing taxpayer compliance; conducted tax policy reviews in several countries, including the IMF's newest member, Montenegro; met a significant increase in demand for advice on resource taxation from a number of resource-rich countries in Africa, Asia, and South America; and supplied advisory services in public financial management, pension reform, fiscal responsibility frameworks, and expenditure rationalization. FAD both organizes and participates in conferences, seminars, and workshops targeting particular countries and in conjunction with specific institutions. For example, a major regional outreach event for European countries on strengthening public investment and managing risks from public-private partnerships was held in Budapest in March 2007.

The Statistics Department's (STA) technical assistance program promotes internationally accepted data standards, with an emphasis on regional projects and collaboration with other donors and providers. During FY2007, STA provided technical assistance and training to a wide range of member countries to support lasting improvements in national statistical systems. The statistical work of the RTACs has been fully integrated into STA's capacity-building program, and as a result STA fielded 431 technical assistance missions during the year, of which 157 benefited African countries. The department also conducted 42 training courses in macroeconomic statistics through the IMF Institute and the IMF Regional Training Centers, in collaboration with various organizations.

Professor Guillermo Calvo leading a seminar at the IMF Institute

The IMF's Legal Department maintained an active technical assistance program during the year directed toward helping member countries strengthen their legal frameworks, particularly in terms of the financial system, taxation and budget management, and anti–money laundering and combating the financing of terrorism (AML/CFT). While demand from member countries for advice in core legal areas (commercial banking, central banking, and taxation) has continued to be high, new areas of focus have also emerged, such as insurance, deposit insurance, nonbank financial institutions, and Islamic banking. The consolidation of AML/CFT activities in the Legal Department has made the department the largest multilateral provider of AML/CFT technical assistance. Support in this area has included policy advice, drafting of legislation, and guidance

55 Although capacity building still constitutes a substantial part of MCM's technical assistance, there is a growing emphasis on assistance in more complex and specialized fields, such as inflation targeting, empirically based stress-testing models, and portfolio management for the public sector.

in establishing or strengthening Financial Intelligence Units (FIUs) and other institutions and supervisory mechanisms. Also, training has been provided to FIU staff, financial supervisors, and ministries of finance and justice officials, as well as to Financial Action Task Force–style regional bodies to improve their capacity to conduct high-level mutual assessments. (See Chapter 2 for more information on AML/CFT.)

Training by the IMF Institute

The IMF Institute, in collaboration with other IMF departments, trains officials from member countries in four core areas: macroeconomic management, financial sector policies, government budgeting, and the balance of payments, including how to strengthen the statistical, legal, and administrative framework in these areas. Over three-fourths of the training benefits low- and lower-middle-income countries. The Institute's programs account for about three-fourths of training for officials delivered by the IMF, including training at the regional technical assistance centers.

In FY2007, the IMF Institute delivered 288 course-weeks, producing close to 9,400 participant-weeks of training (CD-Table 4.4, on the CD-ROM). Relative to FY2006, the number of course-weeks rose by about 1 percent, while the number of participant-weeks fell slightly, reflecting normal year-to-year variation in the average class size.

FY2007 saw the opening of the Joint India-IMF Training Program (ITP), the seventh in the IMF Institute network of regional training centers (CD-Table 4.5, on the CD-ROM). The ITP is dedicated principally to training Indian officials but also admits officials from other countries in South Asia and East Africa.

With substantial cofinancing from local cosponsors and other donors, the development of the regional training centers has facilitated a 50 percent increase in IMF Institute training over the past decade. These centers now account for half of all training under the Institute's program. Training at the RTCs has other advantages: courses can be better attuned to regional needs and foster collaboration within regions.

Training at IMF headquarters continues to play an important role, accounting for about one-third of participant-weeks in FY2007. The headquarters program focuses mainly on longer courses, which are less amenable to regional delivery because of the number of IMF staff involved, but also includes some shorter courses that the IMF Institute is unable to deliver widely through the RTCs. The remainder of the training took place at overseas locations outside the regional network, largely as part of ongoing collaboration between the IMF Institute and regional institutions, and also through distance learning.

The tight IMF budget environment has made it more challenging to meet the training needs of member countries and ensure an up-to-date curriculum. The IMF Institute has responded by increasing workloads and cutting costs, and cofinancing from training partners and other donors has been playing an increasingly critical role.

The IMF Institute training program is reviewed regularly to ensure that it responds to the evolving needs of member countries and supports new IMF initiatives.

Chapter 5

Chapter 5 Governance, organization, and finances

The Fund's Medium-Term Strategy (MTS) calls for a number of reforms in the governance and management of the IMF, including adjusting members' quotas to reflect their role in the world economy more accurately; strengthening communication and transparency; embedding MTS priorities in an output-oriented medium-term budget framework; taking other steps to make the IMF a more cost-effective and efficient institution; and adopting a new income model to place the IMF on a sound financial footing for the long term. Substantial progress was made on all of these fronts during FY2007.

Quota and Voice Reform

The funds for most of the IMF's lending come out of its quota resources—the amounts countries deposit when they join the IMF.[56] Each member's quota is based, in principle, on the relative size of its economy and determines the amount it can borrow from the IMF and its voting power. (As set out in the IMF's Articles of Agreement, each member is allotted 250 basic votes plus one vote per SDR 100,000 of its quota.) Although quotas are reviewed periodically and can be increased when deemed necessary by the Board of Governors (Box 5.1), the distribution of quotas and voting power in the IMF has not kept pace with changes in countries' relative weight in the global economy. Moreover, the share of each member's basic votes in total votes has been diluted by quota increases, from more than 10 percent until the mid-1970s to about 2 percent in recent years.

56 Not all of the paid-in capital is readily available to finance new lending because of the IMF's previous commitments and its policy of lending only in the currencies of members considered financially strong. See the box on the IMF's financing mechanism on the CD-ROM (CD-Box 5.1).

In its communiqué of April 22, 2006, the International Monetary and Financial Committee (IMFC) recognized the need for fundamental reform of quotas and voice in the Fund. It called upon the Managing Director to work with the IMFC and the Executive Board to develop concrete proposals by the time of the IMF–World Bank Annual Meetings in September 2006 for improving the distribution of quotas and voting power to reflect changes in the weight and role of countries in the world economy and to ensure that low-income countries have a voice in the IMF's decision-making process.

An intensive work program followed, involving IMF management and staff, consultations with a broad spectrum of the membership, and discussions in the Executive Board. On August 31, 2006, the Executive Board reached agreement on a comprehensive program of quota and voice reforms and recommended that the Board of Governors adopt a Resolution providing for a two-year plan to implement these reforms. This proposal was transmitted to the Governors by the Managing Director on September 14, 2006, and the Board of Governors adopted the Resolution on September 18, 2006.[57]

In its report to the Board of Governors, the Executive Board emphasized the two main goals of quota and voice reforms: (1) to make significant progress in realigning quota shares with economic weight in the global economy and make quota and voting shares in the Fund more responsive to changes in global economic realities in the future; and (2) to enhance the participation and voice of low-income countries whose weight in the global economy may be small but for which the IMF plays an important advisory and financing role.

The Resolution provided for an initial round of ad hoc quota increases for four countries—China, Korea, Mexico, and Turkey—that were clearly underrepresented, and a set of more fundamental reforms to be delivered by the 2007 Annual Meetings, if possible, or by the 2008 Annual Meetings, at the latest. The reforms are to include (1) agreement on a simple and transparent new quota formula; (2) a second round of ad hoc quota increases based on the new formula; (3) a commitment to ensuring that quota shares continue to evolve in line with countries' changing positions in the world economy; (4) an increase in basic votes of at least 100 percent to protect the voting share of low-income countries as a group, together with adoption of a means to keep the proportion of basic votes in total voting power constant in the future; and (5) measures to increase the administrative resources of the chairs with the largest constituencies.[58]

Box 5.1 Initiation of the Thirteenth General Review of Quotas

The IMF normally conducts general reviews of members' quotas every five years to assess the adequacy of its resource base and to adjust the quotas of individual members to reflect changes in their relative positions in the world economy. The Executive Board completed the Twelfth General Review of Quotas on January 28, 2003, without proposing an increase or any adjustments. The Thirteenth General Review of Quotas was initiated in January 2007 and will need to be completed by January 28, 2008. The IMF's total quotas now stand at SDR 217.3 billion.

In its September 17, 2006, communiqué, the IMFC urged the Executive Board to work constructively and expeditiously on all elements of the reform so as to garner the broadest possible support, underlined the importance of timely implementation, and called on the Managing Director to provide a status report at its next meeting.

Following the 2006 Annual Meetings, the Executive Board began to work on the second stage of reform. In January 2007, it had a preliminary discussion on a proposed amendment to the Articles of Agreement regarding basic votes. Directors found the proposed amendment to be responsive to the Board of Governors' request and generally endorsed the framework proposed by IMF staff. They noted that the number by which basic votes will be increased will need to be discussed and agreed at a later stage, when work on the new quota formula is more advanced. A comprehensive work program involving consultations with the membership and two informal discussions by the Executive Board before the 2007 Spring Meetings of the IMFC was initiated on a new quota formula that would guide the second round of quota increases.

In its communiqué of April 14, 2007, the IMFC welcomed the broad consensus reached in the Executive Board on the legal framework for an amendment of the Articles of Agreement

57 *The Resolution can be found on the CD-ROM, as can Press Releases 06/189, "IMF Executive Board Recommends Quota and Related Governance Reforms," and 06/205, "IMF Board of Governors Approves Quota and Related Governance Reforms." Press releases 06/189 and 06/205 can also be found at* www.imf.org/external/np/sec/pr/2006/pr06189.htm *and* www.imf.org/external/np/sec/pr/2006/pr06205.htm, *respectively.*

58 *On May 9, 2007, shortly after the end of the financial year, the Executive Board agreed to increase by one Advisor the staffing for the Executive Directors representing 20 or more countries (the two sub-Saharan African constituencies). A few Directors underscored that further steps were needed to strengthen the capacity of the Executive Directors' Offices representing the largest constituencies.*

regarding basic votes and the initial work on a new quota formula. It stressed the importance of agreeing on a new formula that is simple and transparent and that captures members' relative positions in the world economy while enhancing the voice and participation of low-income countries. The IMFC also called on the Executive Board to continue its work on the reform package as a matter of priority.

Communication and Transparency

Through its communication strategy and transparency policy, the IMF seeks to increase its accountability to stakeholders and build understanding of sound economic policies. With the guidance and support of the Executive Board, which regularly reviews the IMF's communication strategy and transparency policy, the IMF's efforts in these areas have increased significantly since the mid-1990s.

Communication

While acknowledging that the IMF has made great strides in increasing transparency and communication, the MTS calls for an increase in outreach, emphasizing that bringing about policy change requires active engagement not only with country officials but also with the broader public. During FY2007, IMF staff intensified their efforts in this area and presented a new draft communication strategy for formal Board discussion in early FY2008.

Outreach. The IMF continues to strengthen its outreach to its official stakeholders, while also broadening outreach to other groups, including civil society, legislators, and the private sector. Outreach to these groups has been useful not only in terms of explaining the IMF's positions but also in receiving feedback that can lead to improvements in operations, as has already happened in several areas—for example, the streamlining of conditionality, and the IMF's early support for the Multilateral Debt Relief Initiative and participation in the Extractive Industries Transparency Initiative.

As part of its outreach efforts with civil society and legislators, in recent years the IMF launched a newsletter on its Web site for civil society, and in FY2007 it launched a Web page for legislators that invites the latter to send in their comments and questions.[59] In December 2006, IMF and World Bank officials had a two-day meeting with 55 labor union leaders from around the world on managing globalization and enhancing job opportunities. Outreach events for parliamentarians included a macroeconomic policy seminar for parliamentarians in the Kyrgyz Republic in May 2006, and participation in two conferences in March 2007—a two-day conference in Washington, D.C., for Caribbean parliamentarians and officials of the Inter-American Development Bank (IDB) and the IMF; and the Annual Conference of the Parliamentary Network on the World Bank, which was held in Cape Town, South Africa.[60]

Continuing efforts were made in FY2007 to reach out to the private sector. In February 2007, the Managing Director delivered a speech at the Latin American Business Association Conference, held at Columbia University in New York, and participated in a high-level conference on investment in Central America attended by senior policymakers, major international investors, and business association leaders from Central America and the Dominican Republic.[61] The IMF and the World Bank helped organize the conference, which was held in Costa Rica.

The IMF has been making greater use of seminars and conferences to bring officials and other stakeholders from countries in the same region together to discuss key regional economic policy issues. For example, in December 2006 the IMF and the Arab Monetary Fund jointly sponsored a high-level seminar in Abu Dhabi, United Arab Emirates, on institutions and economic growth in the Arab countries. The IMF also participated in the Fifth Annual Regional Conference on Central America, Panama, and the Dominican Republic, which was hosted by the Central Bank of the Dominican Republic in Punta Cana, in June 2006.[62] The IMF and the Monetary Authority of Singapore co-hosted their second seminar on regional financial integration, in May 2006 (the first seminar took place in September 2005), and the IMF and the government of Singapore jointly organized a high-level seminar for policymakers and economists around the world on crisis prevention in emerging market countries in July 2006 as a run-up to the 2006 Annual Meetings.[63] The Japan Bank for International Cooperation and the IMF cosponsored a conference

59 *The civil society newsletter is posted at* www.imf.org/external/np/exr/cs/eng/index.asp, *and the legislators Web page is at* www.imf.org/external/np/legislators/index.htm.

60 *For more information on these events, see Press Release 06/108, "IMF Macroeconomic Policy Seminar for Parliamentarians from the Kyrgyz Republic," at* www.imf.org/external/np/sec/pr/2006/pr06108.htm; *a speech delivered at the Cape Town conference by the Director of the IMF's African Department, Abdoulaye Bio-Tchané, at* www.imf.org/external/np/speeches/2007/031707.htm; *and Press Release 07/44, "Caribbean Parliamentarians Meet with the IDB, IMF, and World Bank for the first time in Washington, D.C." at* www.imf.org/external/np/sec/pr/2007/pr0744.htm.

61 *The communiqué of the conference is available at* www.imf.org/external/np/cm/2007/020207.htm.

62 *For more information on the seminars on institutions and growth in Arab countries, and the fifth annual conference on Central America, Panama, and the Dominican Republic, see* www.imf.org/external/np/seminars/eng/2006/arabco/index.htm *and* www.imf.org/external/np/seminars/eng/2006/centram/index.htm, *respectively.*

63 *See* www.imf.org/external/np/seminars/eng/2006/cpem/index.htm.

Rodrigo de Rato, IMF Managing Director, speaking to the media at the 2006 Annual Meetings, Singapore

in Tokyo in April 2007 on policy options and challenges for developing Asia; speakers and participants included government officials and academics from low-income countries in Asia. And the IMF and Bruegel, a Brussels-based think tank, organized a joint two-day conference, "Putting Europe's Money to Work: Financial Integration, Financial Development, and Growth in the European Union," in March 2007 for researchers, policymakers, and practitioners from Europe and around the world.

Other examples of outreach activities can be found in Chapters 2 and 4.

Languages other than English. Building on the Report of a Task Force on Publication of Fund Documents and Information in Languages Other than English, which recommended translation of documents for which demand is high into languages heavily used in the IMF's work, a working group of IMF staff was set up to further consider this issue and make concrete proposals. The findings of the Working Group on Publication of Fund Materials in Languages Other than English were presented to the Executive Board in an informal briefing in April 2007, and the IMF has begun translating selected documents—including press releases and WEO summaries—more systematically into relevant languages and posting them on its Web site. The Executive Board also approved the translation of the *2007 Annual Report* into a greater number of languages than in the past, using savings on production costs to achieve this goal.

Publications and the IMF's Web site. An interdepartmental working group reviewed the effectiveness of the IMF's publications program during FY2007.[64] While the review found that the fundamental goals of the program remain valid—sharing IMF research and knowledge in a cost-effective manner—it also found scope for improvement, notably by proposing a more strategic approach to selecting what to publish and how best to deliver it (in print or online or both); increasing marketing efforts (including by entering into partnerships with commercial publishers when appropriate); enhancing the online visibility of the Fund's research publications; establishing an e-commerce site; making greater use of technologies such as print-on-demand; and introducing a differential pricing policy for publications, which will give readers in developing countries greater access to Fund publications.

64 See CD-Box 5.2, "Disseminating information: The IMF's publishing operations and Web site," on the CD-ROM.

Box 5.2 Liaison with intergovernmental, international, and regional organizations

The IMF has a long history of collaboration with numerous international and regional organizations. The IMF's collaboration with the World Bank is especially close. Areas in which the IMF and the World Bank collaborate include the Financial Sector Assessment Program, development of standards and codes, the Poverty Reduction Strategy Paper process, the HIPC and Multilateral Debt Relief Initiatives, and debt sustainability analysis. In March 2006, the IMF's Managing Director and the World Bank's President created the External Review Committee on Bank-Fund Collaboration. The Committee solicited views from member countries on the nature and practice of Bank-Fund collaboration, which has been guided since 1989 by a formal Concordat. The Committee released its report in February 2007.[1]

The IMF also collaborates with the regional multilateral banks—the African Development Bank, the Asian Development Bank, the Inter-American Development Bank, and the European Bank for Reconstruction and Development—including in-country mission work and the provision of technical assistance, and attends meetings of the heads of the regional multilateral banks. The Inter-American Development Bank and the African Development Fund participate in the Multilateral Debt Relief Initiative.

The IMF is a member of the Financial Stability Forum, which brings together government officials responsible for financial stability in the major international financial centers, international regulatory and supervisory bodies, and committees of central bank experts. It also works with standard-setting bodies such as the Basel Committee on Banking Supervision and the International Association of Insurance Supervisors. In 2000, Horst Köhler, then IMF Managing Director, established the Capital Markets Consultative Group to provide a forum for informal dialogue between participants in international capital markets and the IMF; the Group is chaired by the IMF's Managing Director.

The IMF, through its Special Representative to the United Nations, communicates and cooperates with the United Nations and a number of UN agencies. Over the past year, particular emphasis has been placed on supporting the work of the United Nations' new Peacebuilding Commission while the IMF continues to be engaged in the Financing for Development process and to participate in the activities of the UN Economic and Social Council (ECOSOC). Collaboration between the IMF and the WTO takes place formally as well as informally, as outlined in their Cooperation Agreement of 1996. The IMF has observer status at WTO meetings, and IMF staff contribute to the WTO Working Group on Trade, Debt, and Finance, and the Committee on Balance of Payments Restrictions. IMF staff participate in the Integrated Framework for Trade-Related Technical Assistance and the Aid for Trade Task Force (see Box 3.3).

IMF staff also liaise with the Organization for Economic Cooperation and Development (OECD), the Bank for International Settlements (BIS), the European Commission, the Asia-Pacific Economic Cooperation (APEC), and several regional groups in Asia, including the Association of Southeast Asian Nations (ASEAN). The ASEAN Secretariat, the IMF, and the Royal Government of Cambodia co-hosted a high-level seminar in June 2006 on how regional integration could accelerate the development of Cambodia, the Lao People's Democratic Republic, and Vietnam.[2]

The IMF is an active participant in the meetings and activities of the major intergovernmental groups, including the Group of Seven (G-7), Group of Eight (G-8), Group of Ten (G-10), Group of Twenty (G-20), and Group of Twenty-Four (G-24). The G-10 countries participate in the IMF's General Arrangements to Borrow, an arrangement established in 1962 that can be invoked if the IMF's resources are estimated to be insufficient to meet members' needs.

1 *See Press Release 07/32, "IMF Managing Director and World Bank President Paul Wolfowitz Welcome Report on Enhancing IMF–World Bank Cooperation," and the Report itself. Both are on the CD-ROM and also on the IMF's Web site, at* www.imf.org/external/np/sec/pr/2007/pr0732.htm.

2 *See Press Release 06/145, at* www.imf.org/external/np/sec/pr/2006/pr06145.htm.

Box 5.3 Activities of the IEO in FY2007

The Independent Evaluation Office (IEO) was established in 2001 to conduct independent and objective evaluations of IMF policies and activities with a view to increasing the IMF's transparency and accountability and strengthening its learning culture. Under its Terms of Reference, the IEO is fully independent of IMF management and operates at arm's length from the IMF's Executive Board, to which it reports its findings. In January 2007, the Board agreed on a more systematic approach to, and stronger monitoring of, the implementation of Board-endorsed IEO recommendations.

During FY2007, the IEO focused its efforts on the completion of two evaluations: "The IMF and Aid to Sub-Saharan Africa," and "The IMF's Advice on Exchange Rate Policy." The Executive Board discussed the former in March 2007 (see Chapter 3). Following the Board discussion, the IEO presented the report's findings at several international outreach events, starting with a seminar at the African Development Bank in late March. The report has been translated into French and Portuguese. The evaluation of the IMF's advice on exchange rate policy was sent to the Executive Board in March 2007 and was scheduled for discussion in early FY2008. The evaluation explores whether the role of the IMF in exchange rate policy advice is clearly defined and understood, assesses the quality of that advice, and examines the quality of the dialogue with country authorities. While acknowledging that the quality of the IMF's advice to its member countries has improved, the IEO identifies a need to revalidate the fundamental purpose of IMF exchange rate surveillance, thereby clarifying the expected roles of the IMF and member countries, and offers detailed recommendations for improving the management and conduct of the IMF's exchange rate policy advice and interactions with member countries (see Chapter 2).

Work on a third evaluation, "Structural Conditionality in IMF-Supported Programs," continued during FY2007. The report is expected to be finalized and sent to the Executive Board before the Annual Meetings in October 2007.

Four topics were added to the IEO's work program for evaluation over the next two years: (1) aspects of IMF corporate governance—including the role of the Board; (2) the IMF's interactions with its member countries; (3) the IMF's research agenda; and (4) the IMF's approach to international trade issues.

The IMF's Web site is the public's primary source of information about the IMF. During FY2007, the site was redesigned to make it a more effective communication tool, the *IMF Survey* increasingly became a Web-based product, and there was a shift to greater reliance on the Web for dissemination of information and messages to enable faster, more frequent, and more flexible communication between the IMF and its stakeholders.

Engagement with media. A biweekly media briefing by the External Relations Department, instituted in late 1999 and initially intended for media based in Washington, D.C., has since developed into a webcast for journalists around the world. The Online Media Briefing Center, a password-protected multimedia site set up in FY2004, allows journalists to access documents under embargo, participate in press briefings, and receive information and data tailored to their needs. The IMF's operational staff have also increased their contacts with the media.

Transparency policy

The IMF's transparency policy stems from an Executive Board decision in January 2001 establishing the presumption that country documents and policy papers and associated Public Information Notices (PINs) would systematically be published, although publication remains voluntary. The decision followed steps that had been taken since 1994 to enhance the transparency of the IMF and to increase the availability of information about its members' policies, while including safeguards to maintain the frankness of the IMF's policy discussions with members by

Meeting of the IMFC at the 2006 Annual Meetings, Singapore

striking the right balance between transparency and confidentiality. Members may request deletion of information not yet in the public domain that constitutes either highly market-sensitive material or premature disclosure of policy intentions.

Following their discussion in FY2006 of an IMF staff review of the transparency policy, Executive Directors called on the staff to produce annual updates on the policy's implementation for posting on the IMF's Web site. The second annual report on the implementation of the transparency policy, published in February 2007, presents information on documents considered by the Board between November 1, 2005, and October 31, 2006, and published by December 31, 2006, including publication rates for each type of document, lags between Executive Board discussions of documents and publication, deletion of material from documents, and the publication behavior of member countries.[65]

In FY2007, publication of reports on Article IV consultations and use of Fund resources rose for the third year in a row, increasing from 82 percent of total reports in 2005 to 85 percent in 2006. The number of member countries that published all reports on their Article IV consultations and use of IMF resources increased from 136 in 2005 to 142 in 2006. The share of Financial System Stability Assessments (reports produced under the Financial Sector Assessment Program) released climbed to 82 percent, and the publication rates both of documents announcing the policy intentions of countries entering into arrangements with the IMF and of PINs increased to 94 percent.[66]

Management and Organization

During FY2007, the IMF reassessed its risk-management framework, curbed its administrative expenditures, and streamlined its procedures by consolidating or shortening reports, modifying misreporting procedures, and lengthening the intervals between policy reviews. It also sought to enhance its effectiveness through improved collaboration in a range of areas with other international and regional bodies (Box 5.2) and by taking account of the recommendations made by the Independent Evaluation Office (IEO) on Fund policies (Box 5.3).

How the IMF is run

The highest decision-making body of the IMF is the Board of Governors, which is appointed by the IMF's member countries. As set out in the Fund's Articles of Agreement, the Executive Board is responsible for conducting the business of the Fund, and for this purpose exercises all the powers delegated to it by the Board of Governors. The Executive Board is composed of 24 Executive Directors and their Alternates appointed or elected by member countries and has responsibility for the day-to-day oversight of the IMF's work at Fund headquarters, located in Washington, D.C.[67] The Managing Director of the IMF serves as the Chair of the Executive Board.

The Board of Governors consists of one Governor and one Alternate Governor from each of the IMF's 185 member countries. The governor is usually the member country's minister

65 *The report, "Key Trends in Implementation of the Fund's Transparency Policy," can be found at* www.imf.org/external/pp/longres.aspx?id=4040.

66 *The increased transparency of the IMF is widely recognized. In its* 2006 Global Accountability Report, *One World Trust ranked the IMF third out of 10 intergovernmental organizations and fourth out of 30 intergovernmental and private transnational companies in terms of transparency. The report can be read at* www.oneworldtrust.org/?display=index_2006.

67 *The Executive Board's calendar for FY2007 and a description of its main activities can be found on the CD-ROM. General information on the governance of the IMF can also be found on the CD-ROM, in the* IMF Handbook. *The list of Executive Directors and their Alternates on April 30, 2007, is on pages 68–69. The voting power of each member is shown in Appendix IV, on the CD-ROM.*

of finance or the head of its central bank. All governors meet once a year at the IMF–World Bank Annual Meetings. There are two committees of Governors that represent the whole membership. The International Monetary and Financial Committee (IMFC) is an advisory body of 24 IMF Governors (or their Alternates) representing the same countries or constituencies (groups of countries) as the 24 Executive Directors.

The IMFC advises, and reports to, the Board of Governors on matters relating to the latter's functions in supervising the management and adaptation of the international monetary and financial system, and in this connection reviewing developments in global liquidity and the transfer of resources to developing countries; considering proposals by the Executive Board to amend the Articles of Agreement; and dealing with disturbances that might threaten the system. It has no decision-making powers. The IMFC normally meets twice a year, in March or April and in September or October, at the time of the Spring and Annual Meetings.

The Development Committee (formally, the joint Ministerial Committee of the Boards of Governors of the Bank and the Fund on the Transfer of Real Resources to Developing Countries) is a joint World Bank–IMF body composed of 24 World Bank or IMF Governors or their Alternates; it advises the Boards of Governors of the IMF and World Bank on critical development issues and on the financial resources required to promote economic development in developing countries. Like the IMFC, it also normally meets twice a year.

Under the Articles of Agreement, the IMF's Executive Board is responsible for the selection of the Managing Director of the Fund. Any Executive Director may submit a nomination, regardless of nationality, for the position.[68] The Managing Director is appointed for a five-year, renewable term. He/she, in turn, with the concurrence of the Executive Board, appoints a First Deputy Managing Director and two Deputy Managing Directors to provide managerial support, one of whom chairs the Board in the Managing Director's absence. The Managing Director is chief of the operating staff of the IMF and conducts the ordinary business of the IMF under the direction of the Executive Board. He/she is ultimately responsible for all aspects of the internal management and working of the institution and its relations and communications with the outside world. The three Deputy Managing Directors share oversight of the IMF's relationship with individual member countries, chair selected Executive Board meetings, and oversee staff work in specific areas.

The IMF's staff is appointed by the Managing Director, and its sole responsibility is to the IMF. At April 30, 2007, the IMF had 2,005 professional and managerial staff and 673 staff at other levels. Eighty-two members of the professional and managerial staff were resident representatives stationed in Africa, Asia and the Pacific, Europe, the Middle East, and Latin America and the Caribbean, covering a total of 92 member countries. Resident representatives, through their professional expertise and familiarity with local conditions, contribute to the formulation of IMF policy advice, monitor countries' economic performance, and coordinate technical assistance; those in low-income countries take part in discussions on poverty reduction strategies. Resident representatives also alert the IMF and the host country to potential policy slippages, provide on-site program support, and play an active role in IMF outreach, working with different branches of government, civil society organizations, donors, and other stakeholders.

The framework for human resource management in the Fund reflects evolving best practices that are consistent with the mission of the institution and the objective of maintaining the quality and diversity of its staff. The Articles of Agreement state that the efficiency and technical competence of Fund staff are expected to be of the "highest standards," and that, in appointing the staff, the Managing Director "shall . . . pay due regard to the importance of recruiting personnel on as wide a geographical basis as possible." In addition, all staff members observe the highest standards of ethical conduct, consistent with the values of integrity, impartiality, and discretion, as set out in the IMF Code of Conduct and its Rules and Regulations.

Recognizing that the membership must have at its service individuals who understand, through their professional experience and training, a wide range of policymaking challenges that confront country officials and who can offer policy advice appropriate to the circumstances of each of the 185 member countries, the Executive Board has long emphasized and expressed concern about diversity, and has repeatedly called for improvements in the diversity of the staff. The Fund thus makes every effort to ensure that staff diversity reflects the institution's membership, actively seeking candidates from all over the world. It recently established a Diversity Council to further its diversity

68 *On July, 12, 2007, the Executive Board adopted a decision setting out procedures for the nomination and selection of the Managing Director; see* www.imf.org/external/np/sec/pr/2007/pr07159.htm.

Table 5.1 Administrative budgets, FY2005–08[1]

(In millions of U.S. dollars)

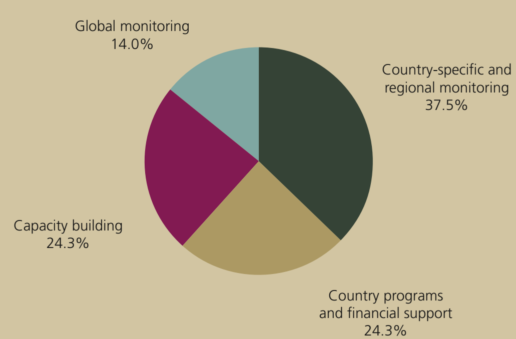
	FY2005 Actual expenditures	FY2006 Actual expenditures	FY2007 Budget	FY2007 Actual expenditures	FY2008 Budget
Administrative expenditures					
Personnel					
Salaries	375.2	392.6	407.5	404.1	424.6
Benefits and other personnel	259.5	273.9	292.7	303.4	298.5
Subtotal	**634.7**	**666.5**	**700.2**	**707.5**	**723.1**
Other					
Travel	90.2	94.2	102.0[2]	93.2	100.5
Buildings and other	167.3	169.6	177.9	159.7	170.2
Subtotal	**257.5**	**263.8**	**279.9**	**258.3**	**270.7**
Gross expenditures	**892.2**	**930.3**	**980.2**	**965.8**	**993.8**
Receipts	(66.1)	(56.0)	(68.3)	(68.5)	(71.4)
Net administrative expenditures	**826.1**	**874.4**	**911.9**	**897.2**	**922.3**

Note: Figures may not add because of rounding.

1 Administrative budgets as approved by the Board for the financial years ending April 30, 2007, and April 30, 2008, compared with actual expenditures for the financial years ended April 30, 2005, April 30, 2006, and April 30, 2007.

2 Includes $5.0 million as a contribution to the costs of holding the Annual Meetings in Singapore.

Figure 5.1 Estimated gross administrative expenditures by key output areas, FY2007



agenda, building on the creation in 1995 of the position of Diversity Advisor. Progress is monitored and problems are reported in a transparent manner in various formats—including the *Diversity Annual Report*—on the IMF Web site. Of the IMF's 185 member countries, 142 were represented on the staff at the end of 2006. Tables showing the distribution of the IMF's staff by nationality, gender, and developing and industrial countries are on the CD-ROM (CD-Tables 5.1, 5.2, and 5.3), as is a table showing the staff salary structure (CD-Table 5.4).

The list of the IMF's senior officers and the IMF organization chart are on pages 70 and 71, respectively, of this *Report*. The organization of the IMF and the functions of its different departments are described in the *IMF Handbook,* which can be found on the CD-ROM.

Box 5.4 Performance indicators

The IMF plans to introduce several types of performance indicators (PIs) progressively, including the following:

- Quantity indicators for all final outputs, and quantity and quality indicators for support and governance activities, along with quality indicators for selected final and intermediate outputs, will be introduced beginning in FY2008.
- Timeliness indicators and other PIs designed to capture the IMF's responsiveness will be phased in over a longer period.
- Further analytical work will be undertaken to examine the feasibility of introducing selected outcome indicators—in particular, intermediate-outcome indicators (regarded as operationally more relevant than final-outcome indicators)—and the need for improved cost-monitoring techniques, to facilitate the use of cost indicators in the budget and business-planning processes.

Work is also under way to introduce supportive information technology applications and to establish a continuous review process for the PIs to help ensure their continued relevance to the IMF's strategy and business model.

Administrative and capital budgets

The administrative budget provides for the personnel and travel costs and other recurrent administrative expenditures incurred by the IMF in providing services to member countries and the international community. The annual budget covers the period May 1 through April 30, the IMF's financial year, and is approved by the Executive Board on a net basis (defined as gross expenditures less receipts).[69] The Executive Board also approves a limit on gross expenditures, based on an upper range of the estimate for receipts. The IMF's net administrative expenditures are funded from operational income, which includes charges on the use of IMF resources, and from reserves.

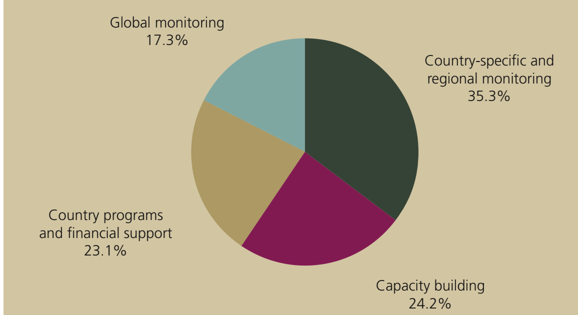
The IMF's capital budget provides funds for capital projects starting in the forthcoming financial year; the projects approved form part of the three-year capital plan that covers all new capital projects. Capital appropriations can be accessed for three years; funds unused at the end of the three-year period lapse.

Budgets and actual expenditures in FY2007

The IMF's administrative budget for the financial year that ended April 30, 2007, authorized total net expenditures of $911.9 million, a limit on gross expenditures of $987.1 million, and appropriations of $48.1 million for capital projects beginning in FY2007. The Executive Board also took note of indicative net administrative budgets of $929.6 million and $952.8 million for FY2008 and FY2009, respectively, and the three-year capital plan of $141 million.

The development of the MTS, the review of the IMF's employment, compensation, and benefits framework, and the IMF's deteriorating income position have changed the institutional and financial environment in which the IMF operates. Accordingly, the FY2007–09 budgets approved by the Executive Board reflected a planned reduction in the overall size of the IMF's real administrative resource envelope and marked the beginning of a downward trend in planned capital expenditures. FY2007 net expenditures were to be held constant in real terms, while the planned FY2008 and FY2009 administrative budgets required real reductions. Notwithstanding the proposed declining real resource envelope, the FY2007–09 medium-term budget (MTB) provided the resources necessary for the IMF to deliver its key outputs—including new MTS initiatives—accommodated by increases in the IMF's internal administrative efficiency and reductions in support-related costs.

Figure 5.2 Estimated gross administrative expenditures by key output areas, FY2008



The outturn on the net administrative budget for FY2007 was $897.2 million, $14.7 million (1.6 percent) less than budgeted. Receipts were $0.2 million above the central estimate on which the net administrative budget was based. Gross administrative expenditures were $14.4 million (1.5 percent) below the $980.2 million central estimate.

Actual administrative expenditures were a little below budget because of slightly lower-than-planned use of resources in the delivery of IMF outputs and a shortfall on certain planned outputs: a small number of projects were delayed, so that the associated expenditures will now be incurred in the current financial year. The resources allocated to the delivery of the IMF's outputs in FY2007 reflected the new priorities identified under the medium-term strategy (Figure 5.1). The new multilateral consultation and the extension of the work of the Consultative Group on Exchange Rate Issues (CGER) to a larger number of countries led to an increased share of gross administrative resources being devoted to multilateral surveillance in FY2007 relative to past years.[70] Relative to FY2006, additional resources were devoted to regional and financial sector surveillance (both MTS priorities), while a smaller share of resources was devoted to work on country programs and financial assistance. The share of resources devoted to capacity building (technical assistance and training) was about the same as in previous years.

In terms of inputs, the gap between budget and outturn reflected a number of factors (Table 5.1). Underlying travel expenditures were about 4 percent ($3.8 million) under budget, and buildings and other expenditures were almost 9 percent ($15.2 million) under budget, the latter reflecting lower

69 Just over half of the receipts consist of external donor contributions for technical assistance to, and training of officials from, member countries; the remainder includes proceeds from publications.

70 Both the multilateral consultation and the CGER's work are discussed in Chapter 2.

building-occupancy costs and less use of contractual services than expected. Personnel-related expenses were about 1 percent ($7.3 million) over budget.[71]

Total capital spending in FY2007 was within the budget for projects approved during FY2005–06. Of the $45.6 million in total capital expenditures, $16.1 million was for building facilities, $5.3 million for the IMF's Headquarters 2, and $24.1 million for information technology projects.

Medium-term budget, FY2008–10

The FY2008–10 medium-term budget approved by the Executive Board on April 25, 2007, allows for an underlying 1.7 percent increase each year, thus implying a real reduction in the Fund's administrative resources for the next three years. Executive Directors agreed that, although a new income model—building on the recommendations of the Committee of Eminent Persons (see "Financial Operations and Policies" below)—must play the major role in putting the IMF's finances on a sustainable footing, expenditure restraint is also necessary. To ensure continued delivery of the IMF's outputs in line with the MTS, the additional resources allocated to meet new needs and priorities of member countries are to be more than offset by savings generated through the increased efficiency of existing operations and by scaling back or eliminating lower-priority activities.

For FY2008, the Executive Board approved a net administrative budget of $922.3 million, with an upper limit on gross expenditures of $998.2 million, and took note of the indicative net administrative budgets of $938.0 million and $959.4 million for FY2009 and FY2010, respectively.[72] The Board also approved appropriations of $46.6 million for capital projects and took note of the medium-term capital plan, totaling $138.0 million.

Continuing the budget reforms that began six years ago, in FY2008 the IMF will begin implementing a full medium-term administrative budget supported by three-year business plans for its departments and offices. In addition, as discussed in Box 5.4, the IMF is introducing performance indicators to assist in monitoring the delivery of departments' business plans. It is also taking measures to improve the accuracy of the systems for allocating costs to specific outputs.

Departmental plans indicate that the reallocation of resources in line with MTS objectives is set to continue under the FY2008–10 medium-term budget. Figure 5.2 shows each output's share of total resources for FY2008.

Box 5.5 Safeguard assessments

The IMF's safeguards assessments policy mitigates the risk that loans made to member countries will be misused. Safeguard assessments aim to provide reasonable assurance to the IMF that a central bank's framework of financial reporting, audit, and controls is adequate to manage its resources, including IMF loans (see CD-Box 5.3 on the CD-ROM). In FY2007, the Fund conducted assessments of 12 central banks in member countries, bringing the total number of completed assessments as of April 30, 2007, to 136. Ongoing monitoring of the safeguards frameworks at central banks continues for as long as members have credit outstanding with the IMF (53 central banks at end-April 2007). Central banks have generally embraced the findings of safeguards assessments, and the safeguards assessments policy has enhanced the IMF's reputation and credibility as a prudent lender while helping to improve the operations and control systems of central banks.

In terms of inputs, the FY2008 administrative budget allows for a 3.3 percent structural salary adjustment (the salary structure as of May 1, 2007, can be found in CD-Table 5.4 on the CD-ROM). Changes to travel policies and practices are expected to hold down travel costs. Expenditures on buildings and other items are budgeted to decline, reflecting targeted reductions in support costs.

Modernizing the risk-management framework

During FY2007, the Advisory Committee on Risk Management (ACRM), established in October 2006 and chaired by Fund management, prepared the IMF's first annual report on risk management based on a Fund-wide survey on operational risks. The report, accompanied by reports on the strategic, core-mission, and financial risks faced by the IMF, was reviewed by the Executive Board and discussed in March and April 2007. Executive Directors considered the report and the underlying work to be an important step in the IMF's efforts to integrate and strengthen various aspects of risk management. They stressed the oversight and critical fiduciary responsibility of the Executive Board for risk management, noting that the day-to-day operational aspects of the IMF's risk-management processes are the purview of Fund management.

71 This overrun in personnel-related expenses was more than accounted for by a special one-off transaction of $19 million, approved by the Executive Board, to accelerate payments into the Staff Retirement Plan (SRP) under a program to provide retirement benefits to staff who were formerly employed on a contractual basis.

72 The nominal figures for both FY2008 and FY2009 are below the indicative figures provided last year, principally because of a reduction in inflation.

The reports presented to the Board constituted a comprehensive assessment of the main risks facing the IMF and the measures in place to mitigate them. The findings were that (1) strategic risks were generally well covered with the Medium-Term Strategy in place; (2) core-mission risks were well covered by the Fund's financial policies and strong oversight and review functions (Box 5.5); (3) financial risks—in particular income risk—are being addressed by shareholders; and (4) measures in place to address the key remaining operational risks (defined as those with a high probability of occurrence or a potentially significant impact) are generally adequate.

Notwithstanding the progress achieved thus far, developing a risk-management framework for the IMF remains a work in progress, to allow the Fund to learn from experience and adapt in a timely way to changing circumstances and any new risks future changes may engender. Such a dynamic approach should help the framework evolve in line with emerging international best practices while continuing to give due consideration to the special character of the IMF as a cooperative global institution and provider of public goods.

Streamlining

In a cost-conscious environment, the MTS proposes streamlining IMF operations and reviewing the allocation of resources to refocus them on more strategic issues while strengthening the quality and effectiveness of surveillance. In FY2007, the Executive Board lengthened the cycle for most IMF policy reviews, consolidated some reports, and eliminated others. To enhance the timeliness of surveillance, the Board shortened the interval between the conclusion of Article IV missions and Board discussions. The IMF experimented with streamlined Article IV consultations (see Chapter 2), and procedures in cases of minor misreporting of data by member countries were modified to make them less onerous for both the IMF and the member.[73] The IMF also reviewed certain support services to identify opportunities for delivering outputs more efficiently and at a lower cost.

Financial Operations and Policies

Income, charges, remuneration, and burden sharing

The IMF, like other financial institutions, earns income from interest charges and fees levied on its loans and uses the income to meet funding costs, pay for administrative expenses, and build up precautionary balances. The current framework relies heavily on income from lending. A priority for the IMF in the period ahead is to establish a new model that generates steady, diversified, and reliable long-term sources of income better adapted than the current model to the broad range of the IMF's activities.

Under the current income model, the basic rate of charge (the interest rate) on regular lending is determined at the beginning of the financial year as a margin in basis points above the SDR interest rate (see Box 3.1). These charges are intended to cover the cost of funds and administrative expenses and to achieve an agreed net income target for the year. For FY2007, however, the Board agreed to (1) keep the margin for the rate of charge unchanged from FY2006, at 108 basis points above the SDR interest rate, and (2) temporarily suspend reserve accumulation.

Since November 2000, the IMF has imposed surcharges on credit extended to discourage unduly large use of credit in the credit tranches and under Extended Arrangements and to preserve the revolving nature of IMF financial resources. The IMF also imposes surcharges on shorter-term loans under the Supplemental Reserve Facility (SRF) that vary according to the length of time credit is outstanding. Income derived from surcharges can be placed in the IMF's reserves or used for other purposes as decided by the Executive Board.

Table 5.2 Arrears to the IMF of countries with obligations overdue by six months or more, by type

(In millions of SDRs; as of April 30, 2007)

		By type			
	Total	General Department (incl. SAF[1])	SDR Department	Trust Fund	PRGF-ESF
Liberia	530.8	472.1	28.1	30.6	0.0
Somalia	233.4	213.0	12.4	8.0	0.0
Sudan	1,033.2	953.4	0.0	79.8	0.0
Zimbabwe	84.7	0.0	0.0	0.0	84.7
Total	**1,882.1**	**1,638.5**	**40.5**	**118.4**	**84.7**

Source: IMF Finance Department.

1 Structural Adjustment Facility.

73 *See PIN 06/95, "IMF Executive Board Modifies Procedures in De Minimis Cases of Misreporting," on the CD-ROM or at* www.imf.org/external/np/sec/pn/2006/pn0695.htm.

Box 5.6 Investment Account

The IMF's Articles of Agreement provide for the establishment of an Investment Account (IA) to generate income to help the IMF meet its operating costs. As part of the review of the IMF's finances and financial structure that began in 2004, the IMF's Executive Board supported the need to broaden the IMF's income base given the decline in demand for IMF lending, until then the main source of income.

The IA was established by an Executive Board decision in April 2006 and funded in June 2006 through a transfer of currencies equal to SDR 5.9 billion from the General Resources Account (GRA). The Articles limit the amount that may be transferred to the IA to the equivalent of the Fund's general and special reserves at the time of the decision to make the transfer. The June 2006 transfer was equivalent to the Fund's total reserves at that time.

Before the funding of the IA, reserves formed part of the currency balances kept with creditor members. The transfer of currencies to the IA therefore increased the reserve tranche positions of creditor members. Reserve tranche positions are remunerated at the 3-month SDR interest rate, the implicit return on the Fund's reserves prior to the IA.

The IMF's objective is for the return on the IA to exceed the return on the SDR interest rate over time while minimizing the frequency and extent of negative returns and underperformance over a 12-month horizon. To achieve this objective, the duration of the IA portfolio is maintained beyond 3-month instruments through investments in eligible longer-term government bonds and other fixed-income securities. External asset managers—including the World Bank, the Bank for International Settlements, and private managers—are entrusted with buying and selling individual securities in accordance with the IA's investment authority, guidelines, and benchmark.

A one- to three-year benchmark index was adopted for the IA. Historical performance suggests that the resulting extension of investment maturities beyond the three-month SDR rate will generate additional income over time.

The IMF also receives income from borrowers in the form of service charges, commitment fees, and special charges. A one-time service charge of 0.5 percent is levied on each loan disbursement from the General Resources Account. A refundable commitment fee on Stand-By and Extended Arrangements, payable at the beginning of each 12-month period under the arrangement, is charged on the amounts that may be drawn during that period, including amounts available under the SRF. The fee is 0.25 percent on amounts committed up to 100 percent of quota and 0.10 percent thereafter. The commitment fee is refunded when credit is used in proportion to the drawings made. The IMF also levies special charges on overdue principal payments and on charges that are overdue by less than six months.

The IMF pays interest (remuneration) to member country creditors on their reserves held by the IMF (known as reserve tranche positions) based on the SDR interest rate. The basic rate of remuneration is currently set at 100 percent of the SDR interest rate (the upper limit permitted under the Articles of Agreement), but it may be set as low as 80 percent of that rate (the lower limit).

Since 1986, the rates of charge and remuneration have been adjusted under a burden-sharing mechanism that distributes the cost of overdue financial obligations between creditor and debtor members. Loss of income from unpaid interest charges overdue for six months or more is recovered by increasing the rate of charge and reducing the rate of remuneration. The amounts thus collected are refunded when the overdue charges are settled. Additional adjustments to the basic rates of charge and remuneration are made to generate resources for a Special Contingent Account (SCA-1), which was established specifically to protect the IMF against the risk of loss resulting from arrears. Effective November 1, 2006, the Board decided to suspend contributions to the SCA-1. In FY2007, the adjustments for unpaid interest charges and the allocation to the SCA-1 resulted in an increase to the basic rate of charge and a reduction in the rate of remuneration of 23 basis points. The adjusted rates of charge and remuneration averaged 5.28 percent and 3.74 percent, respectively, for the financial year.

Income in FY2007 fell SDR 111 million short of expenditures. The net income shortfall largely reflects a substantial decline in IMF credit outstanding, from a peak of SDR 70 billion in September 2003 to SDR 7.3 billion at the end of FY2007, owing to low demand for new IMF credit and advance repayments by some members in recent years. The income shortfall will be offset against the Fund's reserves (retained earnings), which amounted to some SDR 6 billion at end-FY2007. The IMF has taken a number of steps to strengthen its income position. The Board's establishment of the Investment Account in April 2006 and its funding with SDR 5.9 billion in June 2006 were the first steps in diversifying the IMF's sources of income (Box 5.6).

The IMFC recognized the need for more predictable and stable sources of IMF income and called on the Managing Director to develop proposals expeditiously. In May 2006, the Managing Director established the Committee of Eminent Persons to Study Sustainable Long-Term Financing of the IMF.[74] The Committee presented its recommendations to management and the Executive Board in early 2007. At its April 2007 meeting, the IMFC endorsed the report as a sound basis for further work on the development of a new income model for the IMF and looked forward to proposals from the Managing Director for consideration by the Executive Board. Work on the development of the new model is a priority for FY08.

Arrears to the IMF

Overdue financial obligations to the IMF totaled SDR 1.88 billion at end-April 2007 (Table 5.2), 83 percent of which was accounted for by Sudan and Liberia; Somalia and Zimbabwe accounted for the balance. At end-April 2007, all arrears to the IMF were protracted (outstanding for more than six months); 39 percent represented overdue principal, and the rest, overdue charges and interest. More than four-fifths represented arrears to the GRA, while the remainder represented arrears to the SDR Department Trust Fund and the PRGF-ESF Trust. Zimbabwe is the only country with protracted arrears to the PRGF-ESF Trust.

Under the IMF's strengthened cooperative strategy on arrears, remedial measures have been applied against countries with protracted arrears. As of the end of the financial year, Liberia, Somalia, Sudan, and Zimbabwe remained ineligible to use GRA resources. Zimbabwe continued to be excluded from the list of PRGF-eligible countries and is subject to a declaration of noncooperation. In view of Liberia's strengthened cooperation with the Fund, on October 2, 2006, the Executive Board decided to initiate the de-escalation of the remedial measures that had been applied against Liberia and lifted the declaration of noncooperation.

IMF audit mechanisms

The IMF's audit mechanisms consist of an external audit firm, an internal audit function, and an independent External Audit Committee (EAC) that oversees the work of both. The EAC, which also oversees the IMF's accounting, financial reporting, internal control, and risk-management functions, is composed of three members selected by the Executive Board and appointed by the Managing Director. The members serve for three-year terms on a staggered basis and are independent of the IMF. EAC members are nationals of different IMF member countries at the time of their appointment and must possess the expertise and qualifications required to carry out the oversight of the annual audit. Typically, candidates for the EAC come from international public accounting firms, the public sector, or academia.

The EAC selects one of its members as chair, determines its own procedures, and is independent of the IMF's management in overseeing the annual audit. However, any changes to the EAC's terms of reference are subject to Board approval. The EAC typically meets in person in early January, in late June after the completion of the audit, and in July to report to the Board. IMF staff and the external auditors consult with EAC members throughout the year.

The 2007 EAC members are Dr. Len Konar (Chair), Board Member, South African Reserve Bank; Mr. Satoshi Itoh, former Professor, Chuo University, Japan; and Mr. Steve Anderson, Head of Risk Assessment and Assurance, Reserve Bank of New Zealand.

The external audit firm, which is elected by the Executive Board in consultation with the EAC and appointed by the Managing Director, is responsible for performing the external audit and expressing an opinion on the IMF's financial statements based on the audit. At the conclusion of the annual audit, the EAC transmits the report issued by the external audit firm, through the Managing Director and the Executive Board, to the Board of Governors and briefs the Executive Board on the results of the audit. The external audit firm is normally appointed for five years. Deloitte and Touche LLP is the IMF's external auditor.

The internal audit function is performed by the Office of Internal Audit and Inspection (OIA), which provides independent examinations of the effectiveness of controls, governance processes, and risk management. To meet this objective, OIA conducts about 25 audits and reviews a year. OIA reports to IMF management and to the EAC, thus assuring its independence. In addition, the Executive Board is briefed regularly on OIA's work program and the major findings of its audits and reviews.

The IMF's financial statements for FY2007 form Appendix VI of this *Annual Report* and can be found on the CD-ROM as well as on the Fund's Web site, at *www.imf.org/external/pubs/ft/quart/index.htm.* Readers who wish to receive a print copy of the financial statements for FY2007 may request one from IMF Publication Services, 700 19th Street, N.W., Washington, DC 20431.

74 *The Committee's final report was released in January 2007 and is available on the CD-ROM and on the IMF's Web site, at* www.imf.org/external/np/oth/2007/013107.pdf. *The IMF's press release announcing the release of the report can also be found on the CD-ROM, as well as at* www.imf.org/external/np/sec/pr/2007/pr0718.htm.

Executive Directors and Alternates on April 30, 2007[1]

(Alternate Executive Directors are indicated in italics.)

Appointed

Meg Lundsager *Vacant*	United States
Shigeo Kashiwagi *Michio Kitahara*	Japan
Klaus D. Stein *Stephan von Stenglin*	Germany
Pierre Duquesne *Bertrand Dumont*	France
Tom Scholar *Jens Larsen*	United Kingdom

Elected

Willy Kiekens (Belgium) *Johann Prader (Austria)*	Austria Belarus Belgium Czech Republic Hungary Kazakhstan Luxembourg Slovak Republic Slovenia Turkey
Jeroen Kremers (Netherlands) *Yuriy G. Yakusha (Ukraine)*	Armenia Bosnia and Herzegovina Bulgaria Croatia Cyprus Georgia Israel Macedonia, former Yugoslav Republic of Moldova Netherlands Romania Ukraine
Roberto Guarnieri (República Bolivariana de Venezuela) *Ramón Guzmán (Spain)*	Costa Rica El Salvador Guatemala Honduras Mexico Nicaragua Spain Venezuela, República Bolivariana de
Arrigo Sadun (Italy) *Miranda Xafa (Greece)*	Albania Greece Italy Malta Portugal San Marino Timor-Leste
Richard Murray (Australia) *Wilhemina C. Mañalac (Philippines)*	Australia Kiribati Korea Marshall Islands Micronesia, Federated States of Mongolia New Zealand Palau Papua New Guinea Philippines Samoa Seychelles Solomon Islands Vanuatu
GE Huayong (China) *HE Jianxiong (China)*	China
Jonathan Fried (Canada) *Peter Charleton (Ireland)*	Antigua and Barbuda Bahamas, The Barbados Belize Canada Dominica Grenada Ireland Jamaica St. Kitts and Nevis St. Lucia St. Vincent and the Grenadines
Tuomas Saarenheimo (Finland) *Jon Thorvardur Sigurgeirsson (Iceland)*	Denmark Estonia Finland Iceland Latvia Lithuania Norway Sweden

1 *The voting power of each chair can be found in Appendix IV on the CD-ROM; changes in the Executive Board during FY2007 are listed in Appendix V on the CD-ROM.*

Elected *(continued)*

A. Shakour Shaalan (Egypt) *Samir El-Khouri* *(Lebanon)*	Bahrain Egypt Iraq Jordan Kuwait Lebanon Libyan Arab Jamahiriya Maldives Oman Qatar Syrian Arab Republic United Arab Emirates Yemen, Republic of
Abdallah S. Alazzaz (Saudi Arabia) *Ahmed Al Nassar* *(Saudi Arabia)*	Saudi Arabia
Hooi Eng Phang (Malaysia) *Chantavam Sucharitakul* *(Thailand)*	Brunei Darussalam Cambodia Fiji Indonesia Lao People's Democratic Republic Malaysia Myanmar Nepal Singapore Thailand Tonga Vietnam
Peter Gakunu (Kenya) *Samura Kamara* *(Sierra Leone)*	Angola Botswana Burundi Eritrea Ethiopia Gambia, The Kenya Lesotho Malawi Mozambique Namibia Nigeria Sierra Leone South Africa Sudan Swaziland Tanzania Uganda Zambia
Thomas Moser (Switzerland) *Andrzej Raczko* *(Poland)*	Azerbaijan Kyrgyz Republic Poland Serbia Switzerland Tajikistan Turkmenistan Uzbekistan
Aleksei V. Mozhin (Russian Federation) *Andrei Lushin* *(Russian Federation)*	Russian Federation
Abbas Mirakhor (Islamic Republic of Iran) *Mohammed Daïri* *(Morocco)*	Afghanistan, Islamic Republic of Algeria Ghana Iran, Islamic Republic of Morocco Pakistan Tunisia
Paulo Nogueira Batista, Jr. (Brazil) *María Ines Agudelo* *(Colombia)*	Brazil Colombia Dominican Republic Ecuador Guyana Haiti Panama Suriname Trinidad and Tobago
Adarsh Kishore (India) *Amal Uthum Herat* *(Sri Lanka)*	Bangladesh Bhutan India Sri Lanka
Javier Silva-Ruete (Peru) *Héctor R. Torres* *(Argentina)*	Argentina Bolivia Chile Paraguay Peru Uruguay
Laurean W. Rutayisire (Rwanda) *Kossi Assimaidou* *(Togo)*	Benin Burkina Faso Cameroon Cape Verde Central African Republic Chad Comoros Congo, Democratic Republic of the Congo, Republic of Côte d'Ivoire Djibouti Equatorial Guinea Gabon Guinea Guinea-Bissau Madagascar Mali Mauritania Mauritius Niger Rwanda São Tomé and Príncipe Senegal Togo

Senior officers on April 30, 2007

Jaime Caruana, Counsellor

Simon Johnson, Economic Counsellor

Area departments

Abdoulaye Bio-Tchané
Director, African Department

David Burton
Director, Asia and Pacific Department

Michael C. Deppler
Director, European Department

Mohsin S. Khan
Director, Middle East and Central Asia Department

Anoop Singh
Director, Western Hemisphere Department

Functional and special services departments

Michael G. Kuhn
Director, Finance Department

Teresa M. Ter-Minassian
Director, Fiscal Affairs Department

Leslie J. Lipschitz
Director, IMF Institute

Sean Hagan
General Counsel and Director, Legal Department

Jaime Caruana
Director, Monetary and Capital Markets Department

Mark Allen
Director, Policy Development and Review Department

Simon Johnson
Director, Research Department

Robert Edwards
Director, Statistics Department

Information and liaison

Masood Ahmed
Director, External Relations Department

Akira Ariyoshi
Director, Regional Office for Asia and the Pacific

Saleh M. Nsouli
Director, Offices in Europe

Vacant[1]
Director and Special Representative to the Fund Office at the United Nations

Support services

Liam P. Ebrill
Director, Human Resources Department

Shailendra J. Anjaria
Secretary, Secretary's Department

Frank Harnischfeger
Director, Technology and General Services Department

Jonathan Palmer
Chief Information Officer, Technology and General Services Department

Offices

Barry H. Potter[2]
Director, Office of Budget and Planning

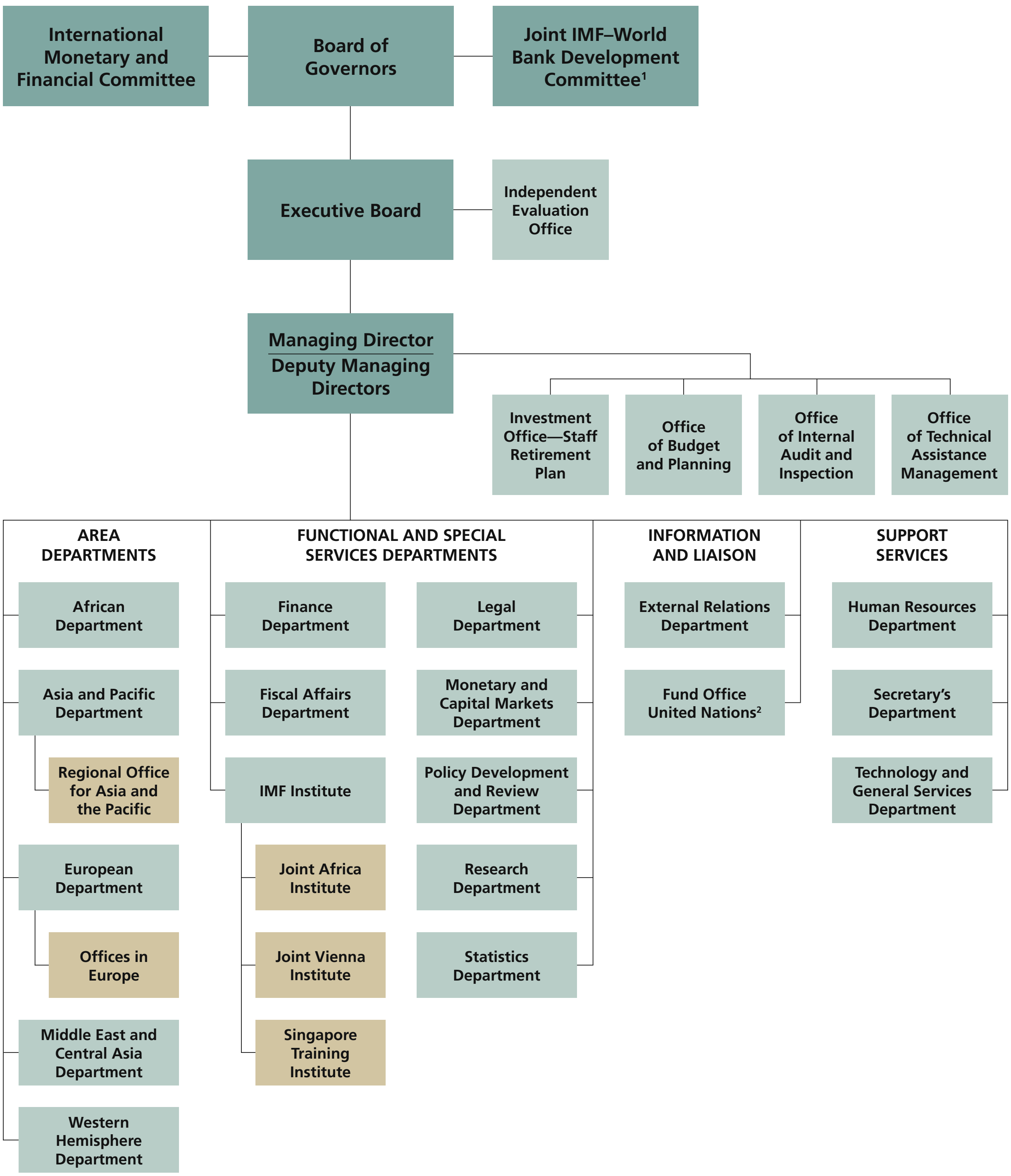
Bert Keuppens
Director, Office of Internal Audit and Inspection

Vacant
Director, Office of Technical Assistance Management

Thomas Bernes
Director, Independent Evaluation Office

1 Barry H. Potter assumed the position of Director and Special Representative to the Fund Office at the United Nations effective August 13, 2007.
2 Siddharth Tiwari succeeded Barry H. Potter as Director of the Office of Budget and Planning effective August 15, 2007.

IMF organization chart as of April 30, 2007



1 *Known formally as the Joint Ministerial Committee of the Boards of Governors of the Bank and the Fund on the Transfer of Real Resources to Developing Countries.*

2 *Attached to the Office of the Managing Director.*

Acronyms and abbreviations

AFRITAC	Africa Regional Technical Assistance Center
AML/CFT	Anti–money laundering/combating the financing of terrorism
APEC	Asia-Pacific Economic Cooperation
ASEAN	Association of Southeast Asian Nations
BIS	Bank for International Settlements
CCE	Coordinated Compilation Exercise
CCL	Contingent Credit Lines
CEMAC	Central African Economic and Monetary Community
CFF	Compensatory Financing Facility
CGER	Consultative Group on Exchange Rate Issues
DFID	U.K. Department for International Development
DQAF	Data Quality Assessment Framework
DSBB	Dissemination Standards Bulletin Board
DSF	Debt sustainability framework
ECCU	Eastern Caribbean Currency Union
ECU	European Currency Unit
EFF	Extended Fund Facility
EMBI	JPMorgan Emerging Markets Bond Index
ENDA	Emergency Natural Disaster Assistance
EPA	Ex post assessment
EPCA	Emergency Post-Conflict Assistance
ESAF	Enhanced Structural Adjustment Facility
ESF	Exogenous Shocks Facility
EU	European Union
EXR	External Relations Department
FAD	Fiscal Affairs Department
FATF	Financial Action Task Force
FCC	Forward commitment capacity
FSAP	Financial Sector Assessment Program
FSF	Financial Stability Forum
FSI	Financial soundness indicator
FSRB	FATF-style regional body
FSSA	Financial System Stability Assessment
FY	Financial year
GDDS	General Data Dissemination System
GDP	Gross domestic product
GFSR	Global Financial Stability Report
GMR	Global Monitoring Report
GRA	General Resources Account
HIPC	Heavily Indebted Poor Countries
IA	Investment Account
IDA	International Development Association (World Bank Group)
IEO	Independent Evaluation Office
IF	Integrated Framework for Trade-Related Technical Assistance
IFRS	International Financial Reporting Standards
IFS	International Financial Statistics
IMFC	International Monetary and Financial Committee
MCM	Monetary and Capital Markets Department
MDG	Millennium Development Goal
MDRI	Multilateral Debt Relief Initiative
MTS	Medium-Term Strategy
OAP	Regional Office for Asia and the Pacific
OECD	Organization for Economic Cooperation and Development
OFC	Offshore financial center
OIA	Office of Internal Audit and Inspection
OTM	Office of Technical Assistance Management
PDR	Policy Development and Review Department
PIN	Public Information Notice
PRGF	Poverty Reduction and Growth Facility
PRSP	Poverty Reduction Strategy Paper
PSI	Policy Support Instrument
PSIA	Poverty and Social Impact Analysis
QEDS	Quarterly External Debt Statistics
REO	Regional Economic Outlook
ROSC	Report on the Observance of Standards and Codes
RTAC	Regional Technical Assistance Center
RTC	Regional Training Center
SAF	Structural Adjustment Facility
SBA	Stand-By Arrangement
SCA-1	First Special Contingent Account
SDA	Special Disbursement Account
SDDS	Special Data Dissemination Standard
SDMX	Statistical Data and Metadata Exchange
SDR	Special drawing right
SRF	Supplemental Reserve Facility
STA	Statistics Department
S&P	Standard and Poor's
TIM	Trade Integration Mechanism
UN	United Nations
WAEMU	West African Economic and Monetary Union
WEO	World Economic Outlook
WTO	World Trade Organization

Credits
This *Annual Report* was prepared by the Editorial and Publications Division of the IMF's External Relations Department. The main editor was Asimina Caminis; composition of the Appendixes was done by Alicia Etchebarne-Bourdin; Teresa Evaristo Del Rosario provided assistance with the preparation.

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INTERNATIONAL MONETARY FUND, 700 19TH STREET, N.W., WASHINGTON, D.C. 20431 U.S.A.

ISBN 978-1-58906-663-2

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IMF Annual Report 2007