

WORLD BANK GROUP

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Statement by the Hon. **NILS BERNSTEIN**,
Governor of the Fund for **DENMARK**, on Behalf of the Nordic-Baltic Constituency,
at the Joint Annual Discussion

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Introduction

1. I am honored to address the 2007 Joint Annual Meetings on behalf of the Nordic-Baltic constituency consisting of Estonia, Finland, Iceland, Latvia, Lithuania, Norway, Sweden and Denmark. Let me begin by welcoming Montenegro as a new member of the Fund.

Financial markets and the global economy are being challenged

2. The global economy continues to expand, powered increasingly by major emerging market countries. Projections for global growth have been moderately reduced in the face of the turbulence in financial markets. But risks are firmly on the downside. Indeed, we have been witnessing the worst credit and liquidity squeeze in world financial markets in a decade. However, economic fundamentals seem to be strong in many parts of the world supported by generally sound policies and skilful liquidity management during the period of turmoil. Reappraisal of risks following periods of very vibrant credit markets is overall sound and good for financial stability.
3. The turbulence in financial markets represents the first real test of structured finance and the related credit derivative markets. With financial globalization, markets are increasingly intertwined, with the effect that external events can have an immediate impact on local markets and institutions. This underscores the importance of strong regional and multilateral surveillance, taking into account spillovers between countries as well as between financial and macroeconomic developments.
4. With its global membership and unique expertise on financial and capital markets, the IMF must take stock and draw lessons from recent developments and integrate them into IMF surveillance. The IMF should be a key player in advocating policies in a timely manner. This will enable its members to harvest the significant benefits of financial innovation and globalization, while the risks can be minimized. Sound macroeconomic policies and developed financial sectors are fundamental elements. Transparency and well regulated financial markets to support confidence deserve emphasis.

Reform of IMF Governance is a pressing issue and viable solutions call for broadly based support

5. One of the political commitments made in Monterrey is solely in the hands of the IMF, namely to enhance the participation of developing countries and transition countries in the decision-making of the IMF. Here, the Fund can set an example that

multilateralism is working.

6. In Singapore, we agreed on a two-year reform of Quotas and Voice to ensure a fair and adequate representation of all members of the Fund. The Fund's legitimacy and credibility rest on meeting the time table and respecting the spirit of the Singapore Resolution. The voice and representation of dynamic economies and low-income countries must be improved.
7. Prior to the 2008 Spring Meeting, we must agree on a new quota formula. It must be simpler, more transparent and based on economically sound principles in order to stand the test of time. We strongly support a compression factor in the quota formula to achieve a balanced and rules-based distribution of quotas. GDP and openness should be the main variables in the formula.
8. No later than by the 2008 Annual Meetings, we must agree to a second round of *ad hoc* quota increases based on the new formula. It should benefit a broader range of the most underrepresented countries in relative terms, and be distributed in a manner that anchors expectations about the nature and direction of future quota increases. At the same time, we strongly support a tripling of the basic votes and a mechanism in the Articles of Agreement to safeguard the share of basic votes in total voting power. We have to enhance the participation of low-income countries.

Reform of the Fund's role in Low-Income Countries is called for

9. Many low-income countries are now achieving much higher growth than in the past. The success mirrors global growth but also that more low income countries have adopted sound macroeconomic policies and reform.
10. The economic progress currently reduces the need for the Fund's traditional balance-of-payments financing. Against this backdrop, it is time for the Fund to review its role. The Fund's work in helping countries absorb the expected increase in aid should receive increased priority in the years to come in close cooperation with other development partners. Also, it will be important to ensure that the countries which have benefited from debt relief do not rebuild unsustainable debt.
11. We continue to believe that the Fund must concentrate its work – also in low income countries – on its core areas of responsibility and expertise. That is, macroeconomic and financial stability advice and help building institutions central to these areas. But this is often closely linked to, *inter alia*, structural reforms, improved quality of public spending and good governance. Thus, the economic challenges in low-income countries call for a clear division of responsibilities and close cooperation between the IMF and the World Bank and other relevant partners in order to attain the Millennium Development Goals.

Reform of the Fund's finances is necessary in view of the changing role

12. The IMF must clarify its role as set out in the Medium-Term Strategy and in line with the fundamental changes in the global economy. Focusing on core areas of expertise will support the Fund's relevance and the resource envelope must be set correspondingly. We must stay firm on the essential need for the Fund to curb expenditures. We expect preparations for taking decisions on proposals, including different compositions and substantial reduction of expenditure. The Fund must practice what it preaches.
13. The current financing of the IMF's activities has a number of shortcomings. It relies heavily on credit intermediation, it is complicated as well as unpredictable, and it draws excessively on a small group of debtors. We welcome the work to find a long-term sustainable financing model for the Fund undertaken by the Committee of Eminent Persons and IMF staff. We endorse the idea that the cost of an individual loan is not set by the Funds overall need for revenue.
14. We believe that a package of measures to better align Fund income with its activities provides a sound basis for discussing a balanced solution. A limited sale of the Fund's gold would provide a good starting point. Naturally, the sale must be ring-fenced and take place in accordance with existing central bank agreements as suggested by the Committee. At the same time, we support prudently enlarging the investment mandate and look forward to study specific proposals. We encourage further analysis of the implications, technicalities and income-generating potential of the proposal to invest the IMF's quota based resources.

Reforms are essential to the Fund's legitimacy

15. For the Fund to be effective and credible, its members must be adequately represented as stipulated in Singapore one year ago. We must clarify the role of the IMF in the 21st century globalization and find a sustainable solution to Fund finances. It seems increasingly pressing to instigate organizational reforms to sharpen the Fund's work and responsibilities - we look forward to discussing the strengthening of governance when the IEO presents its report. A rapidly changing world means challenging times also for the IMF. Being responsive to change is the key to success. We welcome Mr. Strauss-Kahn as the Managing Director and wish him success in this demanding position.
16. We are willing to engage in a reform of the criteria and procedure for the selection process for leading positions in all International Financial Institutions. There is a clear scope to improve openness and transparency of the selection process.

To conclude...

17. The IMF now has 185 members, almost all sovereign countries. This carries with it

an extraordinary responsibility to reflect the world and to provide foundation for global solutions. One area in urgent need of global solutions is the deadlocked Doha negotiations. Let us not forget that the IMF originally was set up to promote international trade by securing a stable and reliable international monetary system. In this spirit, let me use this occasion to urge all countries to bring the negotiations to a successful conclusion.