



STATEMENT BY THE MANAGING DIRECTOR

ON THE INDEPENDENT EVALUATION OFFICE REPORT ON THE IMF FINANCIAL SURVEILLANCE

EXECUTIVE BOARD MEETING
JANUARY 14, 2019

I welcome the report of the Independent Evaluation Office (IEO) on the IMF's financial surveillance. The report recognizes the substantial upgrade the Fund has made in its financial surveillance work since the Global Financial Crisis (GFC) and offers valuable and constructive insights on how to further improve its quality and impact. Accordingly, I broadly support the IEO's recommendations to make IMF financial surveillance more effective.

The IEO report provides a welcome opportunity to reflect on the IMF's initiatives to expand and deepen its financial surveillance work in response to the Global Financial Crisis, which were made explicit in the 2012 Integrated Surveillance Decision and the 2012 Financial Surveillance Strategy. Reflecting its macroeconomic and financial expertise, global membership and governance, the IMF is well placed to make members aware of global financial stability risks while advising them on policies tailored to their circumstances.

I welcome the report's overall findings that the Fund's efforts have delivered a substantial upgrade of its financial surveillance work, including by developing a broad range of diagnostic tools, exploring new policy approaches, and stepping up attention to macro-financial linkages in bilateral surveillance. I am also pleased that the report recognizes that the Global Financial Stability Report (GFSR) and Early Warning Exercise (EWE) are leading sources of insights on the outlook for and risks to the global financial system; and that the IMF is now better prepared to detect financial vulnerabilities and risks.

At the same time, I agree that there remains room to improve the quality and impact of the Fund's work in this area; therefore, I broadly support the report's findings and suggested priorities. I wish to highlight that the 2020 Comprehensive Surveillance Review and Financial Stability Assessment Program (FSAP) Review will provide important opportunities to consider some of the report's key recommendations, while recognizing the constrained resource environment for the Fund. To this end, I appreciate that the IEO identifies areas of highest priority and clarifies that fully implementing all recommendations to meet the IMF's responsibilities and objectives would require significant additional resources. Below is my proposed response to each of the six recommendations presented in the IEO report.

RESPONSE TO RECOMMENDATIONS

Recommendation 1—Strengthening financial and macrofinancial analysis in Article IV surveillance: To improve the relevance and traction of bilateral financial surveillance, the IMF needs to deepen financial and macrofinancial analysis, particularly in Article IV consultations, including by taking practical steps to better integrate FSAP analysis in Article IV consultations and by increasing financial skills and expertise among staff.

I agree with the objective of further strengthening financial and macrofinancial analysis in Article IV surveillance, which resonates with the conclusions of the 2018 Interim Surveillance Review. Further integrating FSAP analysis in Article IV consultations can help achieve that objective. The upcoming FSAP and Comprehensive Surveillance Reviews will consider this recommendation and the related specific suggestions laid out in the report. As major strides in improving financial analysis in Article IV consultations will also require further developing the skillset of country teams, I note that it could entail substantial additional resource costs (see also recommendations 5 and 6).

Recommendation 2—Refocusing FSAP country selection and scope: The IMF should revisit the current approach to allocating FSAP resources to achieve a more flexible, dynamic and risk-based allocation across countries and issues.

I broadly concur with the proposal to review the number of mandatory Financial Stability Assessments (FSAs). Without prejudging the outcome of the FSAP review, I would note that any revised approach to allocating FSAP resources would need to strike a balance among several factors, including evenhandedness and transparency in the selection process; the current voluntary nature of FSAs for most member countries; and the market signaling risks inherent in any selection of countries based on vulnerabilities.

While I agree with the proposal to review the scope and focus across FSAPs (to be considered in the FSAP review), I do not concur with the recommendation to cut back on Fund stress testing in jurisdictions and areas where the authorities already conduct detailed stress tests. The experience so far has shown that stress tests conducted by the authorities in advanced countries vary in quality and

in ambition, while the Fund's independent stress tests have continued to add value in many instances and are integral to the Fund's bilateral surveillance.

Recommendation 3—Increasing traction of multilateral surveillance: The IMF should continue to work to enhance the impact of IMF multilateral surveillance by increasing rigor and transparency, and by deepening collaboration with international partners.

I welcome the conclusion that IMF's work on multilateral financial surveillance is generally well regarded and agree with the recommendation to make more GFSR material available online, subject to copyright constraints. Disclosing more details and data would help improve the traction of the GFSR by ensuring more solid and transparent analytical and empirical backing of Chapter 1 narratives.

I also broadly support the recommendation to deepen collaboration with international partners. In fact, the improved cooperation in recent years between the IMF and the FSB on the EWE has been very successful in achieving the objectives outlined in the report. We plan to continue deepening this cooperation without compromising our capacity to raise out-of-the box issues. However, I continue to believe that further dissemination of the EWE would weaken its effectiveness.

On scaling up the Fund's work with the international regulatory agencies to assess the impact of reforms, the Fund has undertaken several assessments of different aspects of the reforms following the 2012 Financial Surveillance Strategy. Some of these have been conducted jointly with the Standard Setting Bodies (SSBs). We will continue to conduct such assessments, subject to resource availability, while recognizing the challenges that emerge when there is a divergence of views between these regulatory agencies and IMF members that are not represented in them.

Recommendation 4—Enhancing the IMF analytical tools: To enhance the value added of its financial surveillance, the IMF should strengthen efforts to be a global center of excellence on financial and macrofinancial research.

Enhancing the Fund's analytical toolkit is a constant endeavor. Improving the understanding of macrofinancial

linkages remains a high priority for the Fund's multilateral and bilateral surveillance. Exchange of views between the IMF and major central banks can further support that purpose. Furthermore, developing simplified tools and increasing internal outreach to further disseminate existing ones could help strengthen the monitoring of financial risks and assess their implications for financial stability and growth. Staff is currently working on deepening and broadening the application of the Growth-at-risk framework and is developing models to study specific issues related to the intersection of macroeconomics and finance.

The proposal to conduct global stress tests in partnership with the BIS and FSB (see also recommendation 3) is interesting. But I am not convinced that it is feasible, particularly considering the data constraints acknowledged in the report.

With respect to fintech, the Fund is gaining expertise and is active in building international support for cooperative action where appropriate. At the same time, staff is conducting significant analytical work, including recently on central bank digital currencies. These efforts are oriented toward delineating the Fund's role in fintech and focusing on its comparative advantages, in line with its mandate.

Recommendation 5—Building financial skills and expertise: The IMF should intensify efforts to attract, develop and retain a deeper pool of financial talent, as well as to ensure that area department fungible macroeconomists have the knowledge and support to integrate financial and macrofinancial analysis into Article IV consultations.

I agree with the overall message that the IMF has made significant efforts to upgrade the macrofinancial skills of its economists, and that this area remains work in progress. Targeted enhancements from the HR strategy (including a talent inventory and a potential expert track) will help ensure that macroeconomists and experts combine their expertise to support effective macrofinancial surveillance across the membership. The talent management challenges to disseminate and strengthen macrofinancial skills, including through recruiting, will also be considered in the context of the forthcoming comprehensive compensation and benefits review.

Recommendation 6—Increasing budgetary resources: To fully meet its responsibilities and objectives, the IMF should consider devoting significant additional resources to financial surveillance.

I acknowledge that strengthening financial surveillance requires adequate resources. I take note of the recommendation to significantly increase the resource envelope for financial surveillance. Budgetary issues will be considered in the context of the IMF's budget discussions and will need to reflect the areas of the Fund's comparative advantages, medium-term trade-offs, and strategic objectives defined by the Executive Board. In this context, we should also acknowledge the importance of making sure that we assist our members in the most cost-effective way possible.

TABLE 1. THE MANAGING DIRECTOR'S POSITION ON IEO RECOMMENDATIONS

RECOMMENDATION	POSITION
(i) Strengthening Financial and Macroeconomic Analysis in Article IV Surveillance: To improve the relevance and traction of bilateral financial surveillance, the IMF needs to deepen financial and macroeconomic analysis, particularly in Article IV consultations, including by taking practical steps to better integrate FSAP analysis in Article IV consultations and by increasing financial skills and expertise among staff.	SUPPORT
(ii) Refocusing FSAP Country Selection and Scope: The IMF should revisit the current approach to allocating FSAP resources to achieve a more flexible, dynamic and risk-based allocation across countries and issues.	QUALIFIED SUPPORT
(iii) Increasing Multilateral Surveillance: The IMF should continue to work to enhance the impact of IMF multilateral surveillance by increasing rigor and transparency, and by deepening collaboration with international partners.	QUALIFIED SUPPORT
(iv) Enhancing the IMF Analytical Tools: To enhance the value added of its financial surveillance, the IMF should strengthen efforts to be a global center of excellence on financial and macroeconomic research.	SUPPORT
(v) Building Financial Skills and Expertise: The IMF should intensify efforts to attract, develop and retain a deeper pool of financial talent, as well as to ensure that area department fungible macroeconomists have the knowledge and support to integrate financial and macroeconomic analysis into Article IV consultations.	SUPPORT
(vi) Increasing Budgetary Resources: To fully meet its responsibilities and objectives, the IMF should consider devoting significant additional resources to financial surveillance.	QUALIFIED SUPPORT