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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 00/38

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Executive Board Attendance

E. Aninat, Acting Chairman

Executive Directors

A.M. Jul

W. Kiekens

K. Lissakers

A.S. Shaalan

Alternate Executive Directors

A.S. Alosaimi
Y. Moussa, Temporary
P.R. Fenton, Temporary
A. Del Cid-Bonilla, Temporary
J. Schaad, Temporary
W.-D. Donecker

G. De Blasio, Temporary
Vongthieres O., Temporary
A.G. Karunasena

A. Sutt, Temporary
M. Sobel, Temporary
B. Couillault, Temporary
M. Daïri
M.R. Shojaeddini, Temporary
P.A. Akatu, Temporary
S. Vtyurina, Temporary
S. Collins
M. Yépez, Temporary

K. Ongley, Temporary
Tong Y., Temporary
Y.G. Yakusha
H. Toyama

A.S. Linde, Acting Secretary
P. Cirillo, Assistant

**Financial Sector Assessment Program—Progress Report—Lessons from
Pilot Exercise and Next Steps—Conclusion**

Staff representatives: Ingves, MAE; Sundararajan, MAE; Leone, MAE

Also Present

IBRD: A. Bhattacharya, Office of the Vice President; G. Caprio, M. Conthe, and S. Marcus, Financial Sector. Asia and Pacific Department: A. Chopra, R.A. Elson. External Relations Department: L. Aylward. Legal Department: W.E. Holder, Deputy General Counsel; R.C. Baban. Monetary and Exchange Affairs Department: S. Ingves, Director; V Sundararajan, Deputy Director; R.K. Abrams, W.J. Blaschke, L. Errico, P.L.C. Hilbers, C.S. Lee, A.M. Leone, H. Mehran, M.B. O'Brien. Policy Development and Review Department: J.T. Boorman, Director; T. Leddy, Deputy Director; S. Dodzin, J. Hicklin, D.G. Jones, G.R. Kincaid, N.L. Laframboise, Y.A. Metzgen, A. Musalem, M. Rossi. Secretary's Department: P. Gotur. Western Hemisphere Department: M.D. Cerisola. Office of the Managing Director: A. Bauer, J.A.P. Clément, N. Sachdev, T. Wolde-Semait. Assistants to Executive Directors: S.A. Bakhache, A. Jacoby, C. Josz, I. Mateos y Lago, Peh K.H., S. Rouai, C.-P. Schollmeier, M. Walsh.

1. FINANCIAL SECTOR ASSESSMENT PROGRAM—PROGRESS REPORT— LESSONS FROM PILOT EXERCISE AND NEXT STEPS—CONCLUSION

The Executive Directors continued from Executive Board Meeting 00/37 (3/31/00) their consideration of a staff paper on a progress report of the Financial Sector Assessment Program—lessons from pilot exercise and next steps (SM/00/54, 3/15/00; Cor. 1, 3/27/00; and Cor. 2, 3/29/00).

The Acting Chairman made the following concluding remarks:

Executive Directors welcomed the opportunity to review the experience gained so far with the pilot Financial Sector Assessment Program (FSAP). Based on the four cases completed thus far and the other cases presently under way, this pilot was seen as a key element in strengthening the Fund's surveillance and thus a contribution to the ongoing efforts to enhance the international financial architecture. These comprehensive assessments are intended to improve the capacity to identify the strengths, risks and vulnerabilities of countries' financial systems, as well as the interlinkages between macroeconomic policies, economic development and structural issues in the financial sector, and to propose corrective measures and marshal the needed technical assistance. While the pilot was not completed, most Directors agreed that sufficient experience had been gained to draw a number of preliminary conclusions about how to develop further the FSAP.

Directors welcomed the strengthened collaboration between the Fund and the Bank in the context of the FSAP. They noted that this collaboration was contributing to an effective utilization of scarce expert resources as well as providing a platform for policy responses and technical assistance. However, a number of Directors considered that the Fund—with its surveillance mandate—should be uniquely responsible for the surveillance aspect of the assessment of members' financial sectors. In that regard, these Directors argued that the modalities of Fund-Bank cooperation in financial sector work that contributes to the Fund's surveillance responsibilities needed further reflection.

Directors reiterated that assessing the financial sector is an integral part of Fund surveillance. In this regard, many Directors suggested that the FSAP could serve as the primary basis for enhancing the Fund's monitoring of the financial sector in the context of Article IV surveillance. Those Financial System Stability Assessments (FSSAs), derived from the FSAP reports, which the Board has already reviewed, were found to deepen the quality and coverage of Article IV consultations. They provided an in-depth assessment of the strengths, risks, and vulnerabilities of members' financial systems, and also helped in several cases to focus national authorities' attention on financial sector issues which might not otherwise have been subject to close scrutiny.

Welcoming the high quality of the FSSA reports prepared thus far, Directors noted that the FSAP had received widespread support in the global community and at the individual country level. Firm interest in participating in the FSAP in the coming year has already been expressed by national authorities in a number of countries. Directors agreed that the FSAP should be continued and that country coverage could be increased to around

24 countries in FY 2001, although some Directors considered that the number need not be this high. The experience gained over the rest of the pilot phase and the coming year will enable the FSAP and FSSA processes to be further refined. In addition, this will also support the Fund's ongoing efforts to develop a core set of macroprudential indicators.

As regards country participation in the FSAP in the coming year, Directors were pleased that a number of countries had already expressed interest. They encouraged member countries to volunteer to participate, with a view, *inter alia*, to ensuring the widest possible distribution by stage of financial sector development and by region.

Most Directors saw merit in maintaining broad country coverage, noting that small countries and larger industrial countries would both benefit from an FSAP. Given the heavy resource demands of the FSAP exercise, however, some Directors considered that the staff should not aim to cover all member countries. In this connection, they underscored that the FSAP should be targeted to those countries where it could have the most added value; in particular, systemically significant emerging market economies should be given priority.

As regards the scope and coverage of the FSAP/FSSA assessments, an in-depth initial round of assessments should create a solid basis of knowledge so that the ongoing work of financial sector monitoring under Article IV surveillance in a country could be carried out on an annual basis. Pointing to the substantial resource costs associated with the program to date, Directors encouraged the staff to continue to improve the efficiency of the exercise through, *inter alia*, enhanced early planning and focusing the assessments on the key issues in each case.

Directors agreed that assessments of countries' observance of relevant financial sector standards, codes, and good practices should be an integral part of the FSAP in order to help identify and prioritize corrective actions and strategic development plans. Furthermore, such assessments were particularly useful for surveillance if undertaken in the context of the broader assessment of the macroeconomic and institutional setting. Standards observance assessments were also recognized as being resource intensive. Nonetheless, a number of Directors emphasized that standards observance assessments can help to identify areas where reform is needed to strengthen the supervisory and transparency framework. While several Directors cautioned that standards assessments have not been found to be an effective tool for identifying shorter-term risks and vulnerabilities, most Directors emphasized the importance of assessing observance of relevant standards and codes to foster long-term financial stability. Several Directors suggested that stand-alone assessments of observance of financial sector standards, codes, and good practices would be valuable, particularly as the first phase of an FSAP. Moreover, these Directors considered that stand-alone assessments could provide the basis for ongoing monitoring of financial sectors in the context of Fund surveillance. Some Directors considered that summaries of standards observance assessments, which would also comprise the financial sector modules of the Reports on Observance of Standards and Codes (ROSCs), should not be presented as pass/fail assessments for countries' observance of standards.

Directors welcomed the participation in FSAP missions of experts from national central banks and supervisory agencies as well as international standard-setting bodies. Their participation provides an important element of international peer review, especially in the assessments of observance with international standards and codes of good practices. They looked forward to the inclusion of experts from a broader range of institutions in FSAP missions in the future, and encouraged member countries to contribute expert support to the program to the extent feasible. Several Directors encouraged the staff to continue to improve the forward planning of the missions to more effectively utilize experts in the program.

Directors acknowledged that, to be effective, an assessment of a financial system's strengths, risks, and vulnerabilities may require information that is highly sensitive, and it was important to ensure access for FSAP missions to adequate data and information. Further, in order to be willing to provide such information to FSAP missions, national authorities need reassurance that its confidentiality status would be respected. In this connection, most Directors welcomed the Confidentiality Protocol, which sets out procedures for handling sensitive information in both the Fund and the Bank as they relate to financial sector information provided to FSAP teams. They agreed that it would help to clarify with country authorities the details of the confidentiality classifications and related operating procedures. Some Directors were concerned that the Confidentiality Protocol does not go far enough in ensuring the confidentiality of some sensitive material, and the staff was encouraged to review the protocol in light of experience.

On circulation issues, Directors noted that FSAP reports are not circulated to the Board. Several Directors suggested that, in view of the policy recommendations contained in the reports, FSAP reports should be circulated to the Board. A number of Directors were of the view that FSAP documents need not be circulated to the Board, but emphasized that the FSSA documents should report on all aspects of policy advice discussed in the context of the FSAP exercise and relevant to the Fund's responsibilities. In this regard, these Directors stressed the importance of adequate coordination to ensure consistency in the macroeconomic advice given to member countries. FSSA reports will continue to be circulated on a more restricted basis than other general documentation supporting Article IV consultations.

Publication issues arose both in respect of FSAP and FSSA reports. Directors noted that FSAP reports will not be published. They stressed that FSSA reports are Fund Board documents and that the permission of the Board would be required if national authorities wished to publish them. Reflecting the potential sensitivity of the information in, and the conclusions of FSSA reports, the Board has proceeded on the basis that they would not be published. While a few Directors were of the opinion that the Board should give permission to publish FSSA reports, including past cases, it was generally agreed not to grant requests to publish FSSA reports included in the pilot project for the initial twelve cases at this stage. However, as previously agreed, the summary assessments that formed Part II of the FSSA, as they are issued as ROSC modules, can be published on a voluntary basis. With regard to those countries beyond the initial twelve that have already requested participation in the FSAP, it was agreed that strictly informal consultations be undertaken in a timely manner to

clarify views on the possibility that requests for publication of FSSA reports might be permitted following the forthcoming review. The Board will be informed of the results of these consultations as soon as possible. Circulation and publication issues will be taken up again at the time of the next review.

In conclusion, Directors agreed that a further review of the experience under the FSAP should take place toward the end of this year. Management will provide an update on the project for the information of the Board before the Annual Meetings. With the benefit of a larger number of cases, the Board will have a better basis to reach further conclusions on the appropriate modalities of the FSAP.

DECISION TAKEN SINCE PREVIOUS BOARD MEETING

The following decision was adopted by the Executive Board without meeting in the period between EBM/00/37 (3/31/00) and EBM/00/38 (4/4/00).

2. EXECUTIVE BOARD TRAVEL

Travel by Executive Directors as set forth in EBAM/00/46 (3/31/00), EBAM/00/48 (3/30/00), and by an Advisor to Executive Director as set out in EBAM/00/46 (3/31/00) is approved.

APPROVAL: February 8, 2001

SHAILENDRA J. ANJARIA
Secretary