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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 00/12

10:00 a.m., February 4, 2000

Contents

Decisions Taken Since Previous Board Meeting

Executive Board Attendance

S. Fischer, Acting Chairman
E. Aninat, Acting Chairman

Executive Directors	**Alternate Executive Directors**
S.M. Al-Turki	A.S. Alosaimi
A. Barro Chambrier	D. Ondo Mañe
	T.-M. Kudiwu, Temporary
T.A. Bernes	P.R. Fenton, Temporary
	H. Oyarzábal
	J.L. Pascual, Temporary
R.F. Cippà	F. Zurbrügg, Temporary
B. Esdar	W.-D. Donecker
	A.G. Zoccali
	O.A. Hendrick, Temporary
	G. Schlitzer, Temporary
	C. Harinowo
V. Kelkar	A.G. Karunasena
W. Kiekens	J. Prader
O.-P. Lehmussaari	
K. Lissakers	
	G. Bauche
A. Mirakhor	M. Daïri
	C. Rustomjee
	A. Lushin
	S. Vtyurina, Temporary
	S. Collins
M. Portugal	R. Junguito
A.S. Shaalan	A.F. Al-Faris
	J.N. Oh
Wei Benhua	Jin Qi
	Y.G. Yakusha
	I.C. Ioannou, Temporary
	H. Toyama
	M. Yanase, Temporary

S.J. Anjaria, Secretary
A.S. Linde, Acting Secretary
A. Mountford, Acting Secretary
Z.R. Ahmed, Assistant
S.T. Djumena, Assistant

Also Present

IBRD: H. Kharas, R.P. Roulier, East Asia and Pacific Regional Office. Asia and Pacific Department: A. Singh. Deputy Director, W.S. Tseng, Deputy Director; R.A. Elson, L. Giorgianni, R. Moghadam, H. Neiss, U. Ramakrishnan, A. Vamvakidis. European I Department: D.G. Demekas. European II Department: J. Odling-Smee, Director. External Relations Department: T. C. Dawson, Director; G. Hacche, Deputy Director; L. Aylward, D.M. Cheney, J.E. Mark, W.J. Murray, N.V. Shastry. Fiscal Affairs Department: S.E.U. Ahmad, L.U. Figluoli, A.M. Mansour. Human Resources Department: M.G. Prosper. Legal Department: W.E. Holder, Deputy General Counsel; S. Hagan, C.G. Ogada, V.T. Thuronyi. Middle Eastern Department: P. Chabrier, Director; D. Burton, Deputy Director; P. Dhonte, Deputy Director. Monetary and Exchange Affairs Department: C.A. Enoch, O.M.J. Frecaut, R.B. Johnston, H. Mehran. Policy Development and Review Department: T. Leddy, Deputy Director; L.J. Lipschitz, Deputy Director; T.W. Dorsey, P.J. Perone. Research Department: F. Larsen, Deputy Director; E. Jadresic. Secretary's Department: P. Gotur, B.A. Sarr. Treasurer's Department: S.P. Bernhardt. Office of the Managing Director: D.A. Citrin; Office of Budget and Planning: E.-A. Conrad, Director; J. Hudson, P.J. McClellan, M.S. Obias-Bonnefoy, N. Sachdev. Advisors to Executive Directors: P.A. Akatu, J.A. Chelsky, J.C. Estrella, S.S. Farid, O. Himani, J. Jonáš, Luo Y., M.F. Melhem, W. Merz, H. Mori, Nguyen Q.T., A.R. Palmason, M.R. Shojaeddini, M. Sobel, T. Turner-Huggins. Assistants to Executive Directors: J.G. Borpujari, P.A. Brukoff, G. De Blasio, R. Djaafara, K. Gobe, S. Hinata, A. Kapteijn, E. Kornitch, K. Kpetigo, D.H. Kranen, S. Le Gal, W.C. Mañalac, I. Mateos y Lago, Y. Moussa, D. Nardelli, K. Ongley, L. Redifer, V. Rigász, C-P. Schollmeier, A.W. Scoffier, J. Sigurgeirsson, Sugeng, A. Sutt, D. Taylor, Tong Y., M. Walsh, R.P. Watal.

1. REPORT BY FIRST DEPUTY MANAGING DIRECTOR

The First Deputy Managing Director reported on his recent travel to Davos, Switzerland.

The First Deputy Managing Director made the following statement:

> I thought I ought to report briefly on my visit to Davos, Switzerland on the weekend last week, in which I took part in a few public sessions and many bilateral meetings. The main theme in the public sessions was the backlash against globalization, which, in their speeches, President Clinton and Prime Minister Blair turned into what may be an equally relevant issue--a better description of the backlash against globalization--and they called it the problem of exclusion. That is, many groups believe they are being excluded from the process of globalization and find that very difficult to deal with, and that the remedy, which is easier to say than to do, is to begin to find ways of including those who can be included and compensating those who cannot be.
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> I was part of a group known as the informal group of world economic leaders, which discussed globalization with various Prime Ministers and Finance Ministers. A couple of things came out of that. One was a warning not to overreact to Seattle, which was much worse than it needed to be, and that it was not necessarily the case that every international meeting will turn out that bad, with delays in the meeting and so forth. We will be seeing some of that at our own meetings in April, because there will be a very major attempt to disrupt those meetings. I hope we will be better prepared inside, and we are working with the Washington police to try to make sure they are better prepared on the outside as well.
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> It was also said in this meeting that a lot of the issues are not really about globalization, but about changes in domestic economies and increased uncertainties that people faced as well as the increased inequality that you see in many societies. The cures for this lie as much in the area of domestic policy with retraining and related programs to deal with the losers of the process known as globalization, which is really accelerating productivity change, and that we should think a lot more about the necessary domestic policies. In the open meetings a year ago, there has been tremendous hostility against the Fund. I did not feel much of that this time, but I did get into a quite heated debate with the Chief Economist of the World Bank at one of the closed meetings.
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> I will just mention a few of the bilateral meetings I participated in while in Davos. The best reason to go to Davos is that one gets the opportunity to meet with various officials from many countries, and have a chance to hold informal talks, because they do not come with their teams and you do not come with yours.

We met with the South African Finance Minister and central bank Governor, and things seemed fairly good in their relationship with the Fund.

I had a very good meeting with the Finance Minister of Pakistan, who said that we should not judge their policies by what had so far been revealed, and that they did understand that they needed to do something more ambitious than had been on the table so far, and were working on that.

I also met with the Finance Minister of Switzerland mainly to discuss Fund business, to provide an update on the Poverty Reduction and Growth Facility, and to explain what the speech of the United States Secretary of the Treasury about the future of the Fund really meant. There was, as you can imagine, a little bit of discussion about constituency reform as well.

I had a very interesting discussion with the President of Mozambique. I found him extremely impressive in what he had to say, and the way he was thinking about issues.

I met with the Prime Minister, central bank Governor, and Finance Minister of Hungary, where things are going pretty well. In fact, there were some concerns over the fiscal situation, but the central bank Governor told me later that he had found our meeting reassuring, because the Prime Minister had given a variety of assurances to the Fund, which he had not actually given to his own team yet, and the team found that helpful.

I also met with the Foreign Minister of Australia to discuss countries to the north of Australia—Indonesia, Papua New Guinea, and East Timor, the Brazilian authorities, with the Japanese authorities, and with the President of Argentina and his economic team just to discuss the program. This was a very good meeting indeed. The President, who I had met under the same circumstances a year ago, gained in that year tremendous self-confidence, I would say, if that is not presumptuous of me to say that. He clearly has made up his mind on what to do and is committed to doing it, and was doing it a bit faster than we had thought he would do. When we had a small press conference afterward, an Argentine journalist's question was, "how did this all happen so quickly", and my answer was, well, they agreed well before the Fund mission arrived to most of what we would have asked them to do, and there did not remain very much beyond getting the provincial government issue and outer year budget issues dealt with in order to reach an agreement.

I also met with the Deputy Prime Minister of Russia who again, as he had the same day he was appointed, asked for help in putting together the macroeconomic framework from now through the elections, and then for help with the structural reform process after the elections. He was naturally quite concerned about what the Fund mission would do and whether there would be a tranche down the road. I said that it depended on what the mission found, but that the early indications on some of the structural measures were not encouraging and that, as far as I could see, at that moment it was quite possible that we would not complete this review, but that obviously it depended on what we saw. He was concerned about that, and pointed out that Russia has been making payments to the Fund since August I believe without any inflows from the Fund. However, he understood that there were conditions, and we would see whether they had been met. However, the Russian authorities want to get into either a continuation of the present arrangement or a new arrangement after the election if, as most people expect, the present government continues.

I had an interesting meeting with the Finance Minister of Colombia, who said that he had taken the Fund agreement to a meeting with the rebels to explain to them that the Fund of the 1970s no longer exists, and he showed them that there were concerns about social policies in the program and that there was a clause, which you recall, which said that if a peace agreement is signed, various things will be reopened. He said it was actually quite helpful, that the rebels had never looked at such an agreement before, and going through it with them had been quite helpful.

I met with President Kuchma of Ukraine, at the time the story of the charges about Ukraine in 1997 had just come out, and he said, before I raised the issue, that he wanted a full inquiry into what had happened, and would publish its results. Therefore, we will do that. The rest of our talk mainly revolved around reassurances about what they were hoping to do.

I met with the King of Jordan, the Deputy Prime Minister, and the Minister of Planning, and we discussed long-term budget trajectories for Jordan. I realized the value of having a king in these cases, because he could clearly see beyond the next election and a five-year budget stabilization plan was fine with him. I made the case that living from hand to mouth and struggling to meet a budget target each year was not a good way of going forward. I emphasized that they should therefore agree to a medium-term program that would put the deficit on a seriously declining basis, and he was interested in that. His Ministers actually seemed to want that, and they asked us for some help in working on that, so I hope we will be able to get that done.

I met also with the French authorities, including Mr. Trichet, and with the Mexican authorities, including Mr. Ortiz. The Mexicans were very pleased with what is going on, but were a little bit concerned about the strength of the exchange rate, but not terribly concerned.

I met also with the President of Armenia, who used the meetings to have peace talks with the President of Azerbaijan and general talks with the Turkish authorities. He said that if they make progress with Azerbaijan over Nagorno-Karabakh, then the Turkish authorities would be favorably disposed

> to opening up trade more, and he was quite optimistic that that could happen. He also discussed their program with me.
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> The other person that I met was the President of the Kyrgyz Republic, and I believe a paper will be coming to the Board soon.
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> The main reason to go to Davos is not, as I said, the public sessions, but the opportunity to have serious talks at a very high level with a lot of people. The only other thing I would say is that some of you will recall that in 1994 the Middle East and North Africa economic summits were initiated, but were stopped when the Middle East peace process stopped. The summits will now restart, and there was a meeting to discuss that. The next Summit will be held in Cairo. The date is not known, but it will be held sometime in the fall, although that is yet to be confirmed.

Ms. Lissakers asked for more information on the First Deputy Managing Director's discussion with the Chief Economist of the World Bank.

The First Deputy Managing Director replied that the discussion revolved around the usual issues. The Chief Economist of the Bank was expressing his well-known opinions of the Fund, and the customary response had been provided.

2. STRENGTHENING FUND'S EXTERNAL COMMUNICATIONS—PLANS AND RESOURCE IMPLICATIONS

The Executive Directors considered a staff paper on plans to strengthen the Fund's external communications and their resource implications (SM/00/14, 1/27/00).

Mr. Yakusha and Mr. Kapteyn submitted the following statement:

> The last time we discussed our external communications policy in mid-1998, our public image was at an all time low. No doubt, our image has improved somewhat since then, along with the natural cycle of a crisis abating. As economies recover, and the Fund's achievements become more clear, the number of targets for critics to address decreases. There is thus a 'popularity cycle' and we are currently, more or less, on the positive side of the curve. At the same time, however, the Fund continues to be faced by serious public relations challenges, as evidenced, for instance, by the topics that come up in Mr. Dawson's bi-weekly press briefings.
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> The importance of an effective communications policy has become self-evident in recent years. Indeed, we think the External Relations Department (EXR) deserves to be commended for the significant improvements in our communications policy in the past year and a half. Some of the most notable examples, we believe, are the improvements made to our website. The public now has access to the World Economic Outlook (WEO)

database. Country-pages have been set up and hyperlinks are provided to national websites. Mr. Dawson's regular press briefings and the Fund's increased activism on opinion pages are also significant. In addition, of course, the Fund has dramatically increased its transparency by publishing Public Information Notices (PINs), Article IV Consultations, letters of intent LOI's, and Under Fund Review (UFR) statements. This drive towards more transparency and dialogue is consistent with the enhanced role of information and public opinion, in a world of increasingly free and rapid capital flows.

The question is how do we move forward. We certainly welcome today's discussion on External Communication 'plans', but it can only be preliminary. We believe the Board needs to be presented with a full report on the lessons we hope to draw from the Edelman report, and the three more narrow studies. We realize that the results of these reports were informally communicated to the Board, but we have not had a full Board discussion, such as the ones we have had with other external evaluations. Specifically, we would be very interested in the staff's reaction to, for instance, the 48 separate recommendations in the Edelman report. Many of these are very interesting, yet the Staff report does not address them. What does EXR agree and disagree with, and to what should we give priority (the recommendations were made with an unlimited budget constraint)? As page 62 of the Edelman report states, the Fund should not see the 48 recommendations as a rigid program, but as a menu of possibilities from which the Fund should choose according to its own priorities.

The paper before us today does not display 'strategic vision' to the full extent, as advocated in the Edelman report; it merely sums up activities which EXR plans to undertake. EXR needs to make it clear where the present situation is; what should be done in the future; and how plans will be implemented. Answering these questions implies reform. It would also allow us to determine what we can do differently and where we could save resources. As the Edelman report notes on page 29: "the only way, in our minds, to clearly re-prioritize communications in the minds of the Fund staff is to re-organize and re-name EXR". In addition, on page 30: "media relation's effectiveness is hampered by the lack of a clear communications strategy". It is difficult to discuss an increase in resources if the full scope of redeployment is unclear.

This is not to say that we agree with everything the external evaluators have come suggested. Let us provide a few examples of where we think the Edelman report, and, if we understand the staff paper correctly, EXR, set questionable priorities given scarce resources.

It is noted that a strategic plan will be developed for legislatures, particularly the United States Congress. We would agree that it is, for instance, very useful to provide presentations to interested parliamentarians.

Indeed, we repeatedly have small parliamentary delegations visit the Fund from countries in our constituency, and the open discussion they have had with the staff has generally worked extremely well in demystifying the Fund's work and creating a better understanding of what we do. It is another thing, however, to single out the United States Congress by hiring people for a full-fledged communication campaign, devoting significant time and scarce resources to active lobbying. Certainly, some governments have had trouble passing Fund legislation, but this has often been for reasons of political gain, and not because there was a lack of information or access to information.

Similarly, we would be careful in how we target our outreach to civil society, specifically non-governmental organizations (NGOs). Some of these make a living out of criticizing international institutions, and this is a constraint which should be addressed.

It is also not clear what priority should be given to building relations with the private sector. As the Edelman report notes (page 58), this is the sector which views the Fund most favorably. They have a financial incentive to access information—a 'pull' for information, rather than a 'push' by the Fund. We thus do not see why this deserves a 'special' outreach effort. Indeed, market participants indicated that they thought the Fund needed to improve its understanding of the financial sector, which presumably is not EXR's job but that of the policy and area departments.

We suspect that our website (which although very good, could be made more dynamic and user-friendly), bi-weekly press briefings and the 'free media' (interviews, op-ed articles etc.), are the most cost-efficient manner in which to proceed. Their marginal cost is nearly zero while the potential audience is massive. On the other end of the spectrum, paid advertising, as suggested by the Edelman report, can be quite expensive with perhaps little benefit.

Let us offer a few suggestions of what could be considered in a more comprehensive follow-up paper. First, this paper could address more specifically lessons to be drawn from the 4 studies of the communication of management and Directors. The focus in the current paper seems very much on resident representatives and mission chiefs. What could be considered is providing weekly or monthly speaking points for Directors, management, and senior staff on important topics. It is a reality that the domestic press of all countries calls the Fund for comments. Either we attempt to focus our message or we do not. To some extent, Mr. Dawson's bi-weekly press briefing could serve as a guide.

Second, we fully agree that we need to focus on communication by resident representatives and mission chiefs. These are perhaps our main vehicle for giving our communications policy a country-specific focus. A positive example, in this regard, is the way the resident representative has operated in some countries of our constituency. Aside from being in frequent contact with all the main political parties and the local press, they give press conferences immediately following the completion of the Article IV process. Another positive example is the public outreach which the staff has conducted in Indonesia.

Third, the paper could provide concrete suggestions for improving the provision of information to EXR by other departments. Output cannot be improved without good input. We would welcome the appointment of a contact person in EXR for Area Departments. Our own experience is that Area Departments are, at times, completely in the dark when it comes to procedures for publishing documents. In addition, mission chiefs should of course be in contact with their press officer concerning country developments which, evidently, they are not. What EXR could also consider is establishing ties with the offices of Directors. In our office, assistants and advisers cover one or several countries in the constituency and are up to date on a particular country's development.

It should be evident from our comments above that we are sympathetic to an increase in the staff of EXR. As we also noted, however, we do not see how we could specify a specific number without a more comprehensive prioritization of planned activities and indication of possible redeployment and resource savings. Indeed, this is partly why, during the budget discussion, we supported a general staff increase of 105 persons, including EXR, without specifying how much should go to each department. This would allow management to set some of the priorities the Board is unable to set. In keeping with our position in the budget discussion, we cannot approve more than seven people for EXR for fiscal year 200, which is half of what is requested. It goes without saying that we would have no objection, however, to management redeploying the staff from other departments to EXR or using some of the people approved in the general increase. Having said that, however, we would caution against increasing the too quickly and by too much.

Mr. Morais submitted the following statement:

We consider the strengthening of external communications to be important at least in two respects. First, there is need to broaden the appreciation of the surveillance role of the Fund as key to the promotion of the smooth functioning of the international monetary system. Second, there is also the need to build support for the Fund's involvement in economic adjustment and reform within member countries through a more transparent formulation of policies.

Against this background, we feel the conclusion drawn by the staff and management on the recommendations of the consultants and the plan of action set out in the paper is reasonable. We could lend our support to the general thrust of the plan. Accordingly, we would like to make some brief general remarks before commenting on any of the specific recommendations.

Robust Fund advice and work should form the basis for any initiative to strengthen external communications. The resulting soundness of economic policies pursued by member countries would thus speak for itself. The staff and management, as well as the Board should be fully involved in this effort. Hence, the increasing transparency in the work and procedures of the Fund would be important as the Fund proceeds to implement a more effective external communication strategy. In this connection, the message needs to be clear and we should avoid the appearance of trying to engage the institution in a mere public relations exercise to silence the critics. We should instead try to learn from the criticisms.

In general, when the Board decides on some initiative such as the one we are considering today, it is important that we should review carefully the resource requirements. We should then proceed to provide adequate resources for management and the staff to execute the program effectively. In our view, we should minimize redeployment except after careful review of the programs being affected and if a clear advantage and savings have been established.

In contemplating the prospective expansion of the work with other legislatures, especially in African countries, this need not be an on-going and resource-intensive exercise. The Fund could utilize a seminar or workshop format that could involve the member countries' authorities. Indeed, it may be important to help organize such workshops at various political and official levels to clarify the positive development partnership role of the Fund. The PRSP process would also provide a unique opportunity to interact with a wider spectrum of the population in the member country concerned.

Publications, including the material that goes on the Fund's external website should be written in clear language. Here, effort should be made to strike a balance between the nuance, often associated with Fund decisions and procedures, and the clarity that should accompany such documents and publications for public consumption.

We view the involvement of the area and functional department staff to be crucial in promoting and strengthening the external communications effort. In this regard, we see an important role to be played by the Executive Board which may require careful coordination to avoid conflicting messages or duplication.

On page 9 in the last paragraph reference has been made to the commitment by the Board in the explanation of country programs. In the interest of promoting ownership, government programs should ideally be presented by the authorities who are keenly aware of the socio-political perspective or context. It should be left to the authorities to utilize the in-depth knowledge of their Executive Directors to promote greater understanding of the Fund's operations. Perhaps the staff would like to elaborate on the proposition that the Board should assume greater commitment to take responsibility for promoting the Fund within member countries.

Finally, in as much as the plan represents the minimum amount of the recommendations made by the consultants, we would have no difficulty incorporating these into the medium-term budget framework.

Mr. Oyarzabál submitted the following statement:

At the outset, I would like to thank the staff for a useful paper that, in my view, represents a first step in defining a strategy for the Fund's external communications. The recent past has proven that the Fund should be active in educating targeted audiences of its member countries. The scope of the content of the messages that should be conveyed departs from the most basic information of what the Fund is and does to the more complex and delicate issues of surveillance, transparency, and macroeconomic stabilization.

Since the Asian crisis of 1998, the image of the Fund has favorably changed, in part because of the efforts of EXR, as well as the significant turnaround experienced in most, if not all, of the major countries involved or affected by the crisis at that time. It would appear that the messages that are conveyed by EXR hold much greater credibility if countries adjust in a timely fashion and return to stable economic growth.

I believe that the paper before us today has been prepared under pressure to present information to the Board that could be useful in determining resource needs for the year 2001. This would imply that as far as determining a strategy is concerned, a lot more must be done. It is opportune to stress that since the beginning of the discussions of the medium-term resource needs for the institution, I have supported and promoted the need to include resources for external relations. This position not only relates to the importance that this area warrants for the work of the Fund, but also because results from actions of this nature are usually not obtained in the short term. Today our position of support is the same, yet the request for the year 2000 appears to be too high when related to the need to further develop a truly strategic outlook for this activity of the Fund.

Taking into account that preserving and enhancing the credibility of the Fund is essential, the paper does not in effect develop a strategy. It identifies target populations that should be the focus of the initiative. It touches upon certain tasks that also must be carried out. Nonetheless, there are a lot of issues missing that must be taken into account if an effective strategy is to be defined.

Different views of the Fund exist in various countries and regions, which require different communicational objectives and approaches that cannot be generalized for all members of the Fund. It might seem wise to address the academic audience which in many countries helps to form public opinion. This particular sector is not given emphasis in the paper before us.

Nowhere in the paper before us is there mention of the essential need to follow up on all the efforts initiated to measure their effectiveness. This would allow the incorporation of changes to the content of messages, and changes in the targeted audience, or whatever else might be necessary to ensure that the goals are met in a timely manner. I would agree with the recommendation that there “should be an overarching theme in the Fund’s communications, emphasizing that the IMF is effective, responsive, and fair,” is a good one, yet it must be very clear how its effectiveness, responsiveness, and fairness are measured.

The further development of relations with the media reflects a proper approach in strengthening the ties between the institution and that specific audience. It serves the principle of transparency. Through the content of the briefings, it helps to inform the public at large of the analysis, decision-making, or discussions that are taking place within the institution. It would be useful for the staff to be trained to deal with the media, yet when one reads about the possibility of the establishment or definition of media guidelines for the staff in this respect, concern arises about the need to take into account market sensitivities, and political nuances that could affect the relationship based on trust between a member and the Fund.

It appears that greater emphasis is given to the publication of papers in the plan proposed by the staff. Yet it is not clear if this is the most effective way to communicate with the different regions that constitute our membership.

The development of strategies for proactively engaging NGOs merits discussion. In other instances, the legitimacy of NGOs has been questioned. Even if they would appear to be truly representative, how should they be addressed? It would be necessary to define the goal or goals in addressing the varied interests that appear to be present in these organizations. I understand that there are about 15,000 NGOs registered in the US that are politically active, with probably as many interests.

Building a relationship with the private sector confronts highly contrasting realities. The private sector in a country like the United States probably has very different views of the Fund than that of another country in Latin America, Africa, the Middle East, or Asia.

The result of persevering in the application of strong macroeconomic Fundamentals, as well as the efforts by EXR, would lead to having country authorities involved in promoting the Fund more effectively. It would be difficult to reach this objective without a strategy, the development of which would in itself probably be one of the best measures of its success.

In spite of the above comments, I strongly and urgently believe that support must be given to EXR. I cannot go along with the proposal put forth in the paper for 2001. However, I would support a resource allocation of not more than 10 staff positions, in addition to what was approved by the majority for the year 2001 on our last discussion of the medium-term budget outlook.

The Director of the External Relations Department made the following statement:

I appreciate the kind words about the efforts of the Department in the last few months. However, it may be a bit early to declare victory. Though we did not receive criticism in Davos, this is not necessarily a reflection that attitudes have changed. As the Acting Chairman has said in a different context, a Fund-supported program is working when it is no longer called a Fund-supported program: we need to find ways to associate ourselves with the successes that have happened or are happening.

EXR should be understood as performing the function of an informal liaison. We attempt to support a level of activity in the Fund that is determined by other Departments. There are views that perhaps there is not enough of a strategic vision in this paper. What should be understood is that we are in fact responding to the Fund's activities. While we certainly need to explain our approach to the Board, management, and others, it is to some extent derivative. In the paper that was discussed for the medium-term outlook, this vision of what we view the strategy to be is stated.

I note that particular attention is paid in a couple of the statements to efforts regarding NGOs, the U.S. Congress, and the private sector. With regard to outreach efforts to the U.S. Congress, too much can be made of what resource implications are intended. EXR proposed to add one staff member who would spend 75 percent of their time on Congressional issues. The individual who previously was spending 75 percent of their time on the U.S. Congress would spend less time. In a similar manner for NGO activity, adding an additional professional within the Public Affairs Division is proposed.

There was also reference to private sector efforts in both Mr. Yakusha's and Mr. Oyarzabál's statements. Mr. Oyarzabál frames the question correctly when he states the need to have an outreach with the financial sector outside of the United States, which is where our efforts are directed. We have no difficulty hearing from the financial sector in New York, and have been working for some time on reaching the private financial sector outside of the United States. In this regard I recently visited Amsterdam, Germany, and France, as well as Singapore and Tokyo, and will be going to Hong Kong SAR in the near future.

The idea that we need a regional focus in all of our activities is very much our intent. At the same time, this should not be overstated. We are not particularly active in this regard. Our primary role is to assist Fund activities in their presentation to the outside world, but we are not a heavily traveling Department.

Mr. Bernes made the following statement:

For three years I have been saying that the Fund faces a communications problem. We have learned from the consultants that with respect to the private sector, the Fund is misunderstood and greatly feared. The staff has now confirmed that we have a communications problem, and so the question is, what do we do about it.

I have long advocated the need for a much more proactive communications strategy. It is not something which a department such as EXR can do by itself. It involves leadership from EXR, but it really is something that involves the staff, management, and the Board. It involves a change in the culture of this institution, which is similar to a change that a number of other finance ministries and central banks have had to go through. It will take time, and the changes have to reflect the nature of the institution.

I share the thoughts in Mr. Oyarzabál's statement. The paper confirms there is a problem, but does not set out a strategic approach to communications issues. I commend the Director of EXR for the progress he is making, but I agree with him that we cannot declare victory. There is a long way to go.

At the meeting on Wednesday, I shared my views on the overall resource issue and, to reiterate my position, I said that in our view, additions for EXR should have been accommodated within a ceiling of 105 new hires for the financial year 2001. This view was not accepted by Directors. Having argued that this Board should not micromanage Departments by placing precise numbers on specific activities of the Fund, I nonetheless hold the view that EXR needs more resources and is an underfunded activity within this organization. I have proposed the addition of seven new hires, while

Mr. Donecker has proposed more than seven. I am prepared to add ten, balancing the various considerations I have just outlined. Having said that, I would strongly urge the Department to consider rationalizing its current staff resources—the Department has over 80 people already—and look at ways to improve the productivity of existing staff.

On the question of private sector consultation or outreach, I have questions about whether EXR is the appropriate place for this activity. Obviously, there is an outreach part of that activity, but in many ways the dialogue with the private sector is more than just outreach; there is a process of getting information and internalizing that information. It is more of an ongoing dialogue—learning, using intelligence, getting views, and iterating. I am also concerned, given all the other activities that the Director has to undertake and the challenges he is facing, whether he is not already swamped, capable as he may be.

I agree that the staff in area departments and resident representatives need training in media communications. We need to use resident representatives more for the purpose of building relations with the local community. Mission leaders should not shy away from meeting with the local press and, indeed, should be encouraged to do so routinely.

Policy papers and staff reports, particularly on program countries, should begin to include a section on communications issues. In Canada, this is something we routinely do on papers that go before Cabinet ministers—what are the communications issues, what is the strategy, and what is the approach. It forces discipline and it ensures integration between communications efforts and substantive work.

Lastly, I would urge the Fund to improve its efforts at publishing in languages other than English.

The Acting Chairman asked Mr. Bernes what he meant exactly by his suggestion to include a section on communications issues in the staff papers. Was the reference to Fund communications about programs, or what the Fund was doing in a particular country in general with regard to communications?

Mr. Bernes answered that he was referring how best to communicate challenging program or policy issues. The consultants had said that there were too many diffuse messages coming out of the Fund when one or two agreed-upon messages should be determined and persistently emphasized. A section on communications issues would identify challenges with regard to a particular program or policy issue to determine what message should be sent out, and to identify who was in charge of that message.

Ms. Lissakers said that it would be very useful if the Board had access to whatever press guidance was given to the Fund's spokesperson for particular meetings on country matters. While Directors would not be bound to use them, it might nonetheless be worthwhile to know what the spokesperson was saying.

The Acting Chairman considered that it would be useful if the same press guidance given to the staff was given to Directors to explain how the Fund was trying to deal with a particular issue. The problem with including that kind of information in a staff report was that it might be published, but the Board could be informed in some other way.

Mr. Esdar made the following statement:

> I understand that our discussion today is intended to focus on procedures and channels of external communication, on finding the appropriate means of communication and priorities and on the budgetary repercussions. This is certainly appropriate, and I do not have any problems with this approach. However, we have to come back to the substantive questions, in following up on our discussions in July 1998. Based on our considerations on the future role of the Fund, we have to define and to agree upon the general message this institution should give to the outside world. The external evaluators emphasized the need to develop a clearly focused message in this regard. We have to fill this recommendation with concrete input.
>
> In general, I can go along with the suggested initial plan of action. I welcome the strengthened emphasis on improved communications with the media, opinion leaders and opinion makers, and also civil society. The decision to nominate a spokesperson has already borne fruit. Regular or routine press briefings by management will help to explain our objectives and problems. Our outside world coverage has to be universal. It is not sufficient to concentrate on certain markets or media centers. Abu Dhabi, Buenos Aires, Canberra, Seoul, Cairo and Helsinki are of similar importance as Washington, London and Paris.
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> I also would endorse that communications and external relations should not and cannot be limited to the External Relations Department. Improved communication to the outside world should be an objective for the entire staff and become an element of the general job description. Insofar, I would reiterate my position to put more emphasis on these skills during the recruitment process. Finally, also the Executive Board has a significant role in this regard, which can certainly be improved.
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> The staff paper also emphasizes developing strategic plans for working with member countries' legislatures, which seems to be somewhat of a synonym for the U.S. Congress.
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> I certainly agree that our communications strategy should also address a broader spectrum of decision-making bodies beyond member governments. However, the Fund's role in this regard can only be a complementary one.

The primary responsibility to talk to the parliament, parliamentary committees or other institutions inside or outside the official policy decision-making process has to remain with the member country's government. The Fund—beside its general communication policy—should only offer a helping hand.

The plan of action also focuses on publications. I have to admit that here I have some question marks. The Fund already publishes tremendous amounts of paper and information via books, articles, or its website. The issue here seems to be rather to do less more effectively than to do more. Also, I am afraid that some of those who are most opinionated with regard to the Fund, are the least willing to read. Otherwise, some of them would not be so ill-informed and badly focused.

However, I agree that there is an urgent need to make our messages easier to understand and less technical. Reservations with regard to Fundese have frequently been voiced. This refers to the writing of all the staff, but External Relations should aim to provide leadership, since it is they who have to sell the message.

In this regard, I have one particular point which might be the beginning of a phobia. We have to address the problem of acronyms. Quite recently I saw a 35-page paper on Uganda where the list of acronyms and abbreviations covered 1.5 single-spaced pages. I doubt whether the outside world understands what is behind FSAP, FSAA, ROSC, PRGF, PRSP, PRS, DSA, FDI, HIPC, NPV, PFP, etc. I ask External Relations—and not EXR—to join in the fight against this nonsense.

This brings me to the budgetary consequences. There is no doubt that strengthening External Relations requires strengthening its resources. However, there seems to be some additional room for redeployment and streamlining in External Relations as well, particularly so in the area of publications. I could imagine that we could outsource some of the tasks like the bookstore and the distribution of publications. I would invite the staff to look into these possibilities.

With regard to concrete numbers, some colleagues suggested on Wednesday, at least implicitly, a range by introducing a comprehensive staff ceiling of 105 for new hiring which includes External Relations. There is also some flexibility in the budget framework we agreed upon on Wednesday to transfer additional resources to External Relations, using the "Others"-category. In my view, this suggestion seems to be reasonable; however, 105 is not a magic number and should be flexible.

Mr. Portugal made the following statement:

Like previous speakers, I also recognize that we have an urgent need to strengthen and upgrade our policy and our activities in the area of communications. I agree with most of the proposals included in the document. As the document says, it seems that our strategy is conservative and out of touch with the current times, but I also sense that there has been considerable progress in the last year in improving our communications. I would like to recognize and to congratulate the Director of EXR for that, although I agree with him that we cannot yet declare victory.

As indicated, the Fund's image is not a favorable one and also compares unfavorably with many other international organizations. I am convinced that most of this is because of a lack of communication and lack of external players understanding what the Fund does. But should also realize that this is not the only reason for our image. We have to realize there are different political views, different perceptions, and different political interests which no amount of communication might be able to change.

The second reason for the lack of a good image could be mistakes in like any other organization might have made. Mistakes that governments make are often attributed to us, along with the general results of our policies and programs. I mention this point just to be fair with our colleagues in EXR, recognizing that we should not expect them to solve this problem completely.

We should provide more timely information, and have a clearly defined strategy that is consistently applied throughout the organization. Regular briefings and our expanded web site are steps in the right direction, and we should publish material in languages other than English.

I am generally in favor of a more general rather than a targeted approach to external relations, although I recognize that in some particular circumstances and in some specific issues a targeted approach can be useful. A targeted approach has to be carefully designed to suit circumstances to avoid being interpreted as an attempt to co-opt or silence groups.

With respect to the plan for building relations with the private financial sector, as Mr. Yakusha said in his statement, this may not be of great urgency given that the Fund's image is already good and that firms have a special interest in seeking information from the Fund even if we do not make a concerted effort to reach out to them. Nonetheless, it is important to have an institutionalized way of conducting these relations with market participants rather than having a random approach.

It should be considered that it might be better to organize external relations along policy issues, or general themes, rather than along country issues.

> It has been said that EXR plans to develop contacts with NGOs and other civil society representatives in developing countries with the assistance of resident representatives. During the discussion of the PRSP paper, many Directors expressed doubts about this idea because NGOs face three problems of legitimacy, accountability, and efficiency. While governments have developed mechanisms through the years—like elections, parliamentary and judicial oversight, accounting departments, and several levels of government with all sorts of checks and balances—this is not the case with NGOs. Efforts directed toward NGOs have to be part of our overall strategy to this problem and not just a communications issue. Communications should be a consequence of what we decide to do in this area.
>
> Emerging market countries are an important part of our communications strategy. If the Fund has a good image in a program country, the Fund's overall credibility and good image spreads to industrial countries. I agree with Mr. Bernes that a mission chief should not be afraid of having contact with the press, and I welcome the plan to provide training for resident representatives and mission chiefs in this area. Despite training, risks are still large, especially with regard to the resident representative. The resident representative has functions that are similar to an ambassador. Like ambassadors, they should be careful when they express opinions on affairs of the country in which they reside to avoid getting entangled in an internal political debate.
>
> Finally, on the question of additional resources, as the paper mentions, the staff assigned to EXR has been growing at a slower pace than the staff in general, and it seems that we have a lower proportion of the staff dedicated to this activity compared to other international organizations. On the other hand, the number of additional staff that is proposed seems to be large, especially as it adds to the overall increase that we have already approved. Like Mr. Bernes, I wonder if it is possible to have some redeployment, and welcome comments from the staff.

Mr. Barro Chambrier remarked that it was not possible to have a general approach to communications in all cases. Countries with different levels of development required different messages.

Mr. Prader, in response to Mr. Portugal, announced budgetary figures. In nominal terms, the financial year 1998 budget outturn was US$495.3 million and the financial year 2002 estimate under Option 2a could be on the order of 680 million, for a change of some 37 percent. In real terms, the change could be well below 30 percent or perhaps about 3-5 percent per year. Estimates were tentative because the Board had not agreed to an increase for 2001. Nonetheless, there was an underlying expansion occurring.

Mr. Portugal said that when he had mentioned that a general approach was preferable to a targeted approach, he was not referring to countries. There should be a different communications strategy for each country. What was questionable was whether groups should be targeted. For instance, if NGOs were targeted, what began as a communications strategy could deteriorate to a sort of co-optation strategy. To some degree that had occurred at the World Bank which was perceived as having co-opted some NGOs.

Mr. Esdar stated that if the Fund wanted to send a credible message, that message had to be the same for all countries. It could not be defined for particular countries because it would confuse both markets and the public, though the communication strategy could cater to particular countries.

Legitimacy and accountability of NGO's were certainly in question, Mr. Esdar said. Nonetheless, the Fund was confronted with public opinion, which was very much driven by NGOs. At some point, the Fund needed to develop a coherent strategy for dealing with NGOs.

Mr. Shaalan made the following statement:

> First, I would like to thank the staff for preparing a concise and clear paper on the activities and the proposed strategy for the Fund's external relations. I find the paper's approach particularly helpful, as it allows the Board to consider the proposed new strategy along with its staffing implications. The use of such an approach, where possible, should certainly help the Board minimize the type of contentious issues or discussions we have had on the budget over the recent past.
>
> It is unfortunately correct that the Fund's public image is poor, but I would like to point out, and some other colleagues have hinted at this, this is in large measure because of the nature of its activities. It is difficult to compare the Fund with the Red Cross and get an accurate reading of the popularity of each. While carrying out the objectives set in the staff paper—namely, strengthening and professionalizing the Fund's public relations effort—could very well go some way in promoting a better understanding of the institution, we should, as Mr. Portugal reminded us, be under no illusion that our poor image will suddenly be erased if we increase the number of EXR staff. Regardless of how much is spent, the image will not be totally erased. But there is definitely great advantage in providing a better understanding of the activities of this misunderstood institution. The mission of External Relations is a sensitive one, and we should spare no effort in ensuring that the overall strategy is well designed and is backed with sufficient resources. As Table 2 in the paper clearly indicates, the output of External Relations has gone up considerably in the past decade, while the increase in resources during the same period was in no way commensurate with this increase in activity.
>
> While we are in general agreement with the objectives set out in the paper, we would like to highlight, in particular, the importance of coordinating

> External Relations activities with relevant Departments in the Fund. Although coordination will consume the time of the staff in the area departments, such coordination is necessary for the effective representation of the Fund, and we welcome that the envisaged strategy places a high priority on this area.
>
> With respect to relations with civil society and NGOs, care needs to be exercised with respect to the scope of such contacts. We are planning to add one staff member to focus on these contacts, which I assume ensures that we limit the scope of these contacts which can take place in a variety of ways. The most common forum will be meetings called for by External Relations on a particular subject to which NGOs are invited. This will enable both sides to exchange views in an efficient manner. However, when contact is initiated by NGOs themselves through a request for specific meetings or through correspondence, the staff would need to exercise a high degree of selectivity. The exercise can take far more time and resources than is desirable or warranted. We trust that with regard to these contacts special attention will be paid to maintaining the confidentiality of the Fund's information.
>
> Finally, with respect to the level of the requested increase in staff for EXR, I find it difficult to come to a judgment on the proposed increases for the outer years and will only address financial year 2001. During the discussion on the budget last Wednesday, we were among those Directors who viewed that the increase in the staff resources did not include External Relations. We can therefore support an increase that is in addition to the overall figure already agreed upon. As to the magnitude of the increase, I would note that the present revised proposal is significantly below the original proposal, and we have no problem with supporting the request. However, we are prepared to join the majority view in the event that it is different from the proposal by management, but with one qualification. As Mr. Bernes mentioned, the Director of EXR is attempting to do too much at the same time. Whatever cuts are made, I hope none are made from the requested number of the staff.

Mr. Prader noted that according to an article in *Foreign Affairs*, 70 nongovernmental organizations were registered with the United Nations 10 years ago, 7,000 three years ago, and an estimated 15,000 at present. How could one additional staff member handle all of them? He or she would not be able to deal with 15,000 organizations, and it was important not to direct work in a biased manner.

The Acting Chairman asked if Mr. Prader's comments indicated support for an increase in the budget.

Mr. Prader answered that he supported an increase in the budget if the number was reasonable.

Mr. Oh made the following statement:

Like other Directors, I also thank the staff for the preparation of a comprehensive, yet concise paper, and welcome the discussion on resource requirements for the Fund's external communications. However, I would have preferred to have this meeting before, if not in conjunction with, that on the medium-term resource estimates. As it is, the piecemeal approach adopted has hampered the Board from arriving at a more efficient estimate of resource requirements as the overall impact on the budget is not taken into account.

Having said that, I agree with the thrust of the staff paper. I support, in principle, the need to strengthen the Fund's external communications strategy in an effort to increase openness and transparency, and to explain the work of the Fund to a wide range of audiences as a result of the increase in public attention on the Fund's activities over recent years. However, while I support the activities outlined in the action plan, implementation of the activities would not necessarily entail the need for 17 additional staff members. Like Mr. Bernes, Mr. Portugal, and Mr. Shaalan, great effort should be made to reorient existing resources to perceived priorities.

As stated in the paper, coordination among the various departments, including a more active role for resident representatives, can be enhanced to improve external communications. Moreover, it is envisaged that the Board will be asked to commit itself to take responsibility with the authorities for promoting the Fund more effectively within their own constituencies. In this connection, while plans have been made for the Board to play a more active role in external communications, no operational details have been given. The staff's comments on this issue would be appreciated. Similarly, the staff's planned outreach to authorities in capitals might be a worthwhile investment. as it could provide the means for communicating Fund-related issues to their respective audiences.

Finally, the staff has identified a list of measures to be taken, but the staff was silent on what the expected outcomes are in terms of the different audiences. To my mind, some performance measures are needed to assess whether the work program has been successful in improving the Fund's external profile.

Mr. Wei made the following statement:

We broadly agree with the main thrust of this concise paper which, nevertheless, provides us with a lot of information on the status and development plan for the Fund's external communications. We understand and appreciate that EXR has made great efforts in promoting the Fund's image in the international community. However, because of a lack of staff resources, the department is not able to take a more proactive role in implementing their responsibilities which are of great importance to our institution. In this sense, I can generally support the proposal to increase the necessary staff so that EXR can do a better job.

First, we agree with Mr. Morais that the robustness of Fund advice and work should form the basis for any initiative to strengthen the Fund's external communications. In light of this, I believe the staff, management, and the Board should work closely together so that the Fund will be able to provide the most appropriate policy advice to its member countries.

Second, one of the lessons which we could probably draw from the recent financial crises is that the conditionalities attached to Fund-supported programs should be realistic, particularly in the sense that social stability must be taken into full account when they are designed. In this way, we could probably avoid many controversial views. We have to acknowledge that the Fund has paid a heavy price for such controversies.

Third, like others, we believe that it is sufficient and economic for the Fund to explain its work through the internet. Obviously, much can be done to further improve the Fund's web site. Given the Fund's diverse membership, we strongly support the staff proposal that non-English languages be used on the site. We also support the strengthening of the Fund's publication program with the aim to publish more titles for a wider audience. The guiding principle for Fund publication should be driven by demand and not by supply.

Fourth, like Mr. Yakusha, we have some concerns that EXR is proposing to set aside particular staff to work with the U.S. Congress. I am not questioning the important role that member countries' legislatures play in supporting the Fund's work, but it seems to me that such a job should be carried out by the member country's administrative authorities.

I also share Mr. Yakusha's view that we should be careful how we target our outreach to civil society, specifically to NGOs.

Lastly, other departments can also do much by way of propaganda. For example, Research Department staff usually send their representatives to member countries to present the World Economic Outlook (WEO). We find this practice very useful. Along these lines, greater coordination between EXR and other departments could be considered.

Finally, could the staff give us a brief picture of the role played by the World Bank's EXR?

Mr. Al-Turki made the following statement:

I think we all agree on the importance of the Fund's external communication. With heightened interest in the institution, it is crucial to better explain the rationale and benefits of the Fund's work and policies it recommends. The Fund has already taken a number of steps in this respect as detailed in the paper. As a result the number of external relations staff increased by 13 percent in the past 2 years compared to 5 percent growth for the Fund as a whole. While more effort is still needed as evidenced by the external consultants' report, it is important to keep in mind the following.

First, it is unrealistic to expect the Fund to get the same favorable rating as a charitable organization as pointed out by previous speakers. Fund conditionality involves some difficult choices such as fiscal cuts, high-interest rates, and structural reforms that are bound to controversial.

Second, the Fund should not view all criticism as a lack of understanding of Fund policies which can be addressed by a more aggressive external communications blitz. Some of the criticism may be valid and should be taken into consideration when designing Fund policies and recommendations.

Third, it is essential that in the effort to strengthen external communications and increase our contacts with financial markets, confidentiality is not compromised.

Fourth, I agree with Messrs. Portugal and Shaalan regarding contacts with the NGOs.

That said, I can go along with the action plan detailed in the paper. While, it is difficult to determine the exact number of additional staff needed, the request by EXR for 14 staff does not seem unreasonable but I could go along with the consensus on this point. Here, I welcome the staff's detailed presentation on why and where the new staff are needed.

Mr. Zoccali made the following statement:

At the outset, we support the proposition that the Fund should adapt to the global 24 hour news cycle and to the upward trend in the transparency of public institutions generally. We commend management and EXR for the recent steps taken to strengthen the Fund's external communications based on the recognition of the need for this institution to become more proactive and less scholarly and restrained in communicating its message.

With that objective in mind, we have supported those recent initiatives to develop the Fund's communications, which included an increase in resources by six staff in 2000, redeployment to facilitate a more proactive approach to explain Fund operations, and the use of outside consultants to help develop a strategy to improve its public image.

In that context, the Edelman/Wirthlin study provides useful recommendations. However, even if these are fully carried out they should not be considered a sufficient condition for improved public perception given the nature of the Fund's mandate, which, as Messrs. Portugal and Shaalan have already noted, includes conditionality in the form of preventive or corrective measures to promote more stable financial market conditions and orderly adjustment.

As referred to in the Awanohara Study, it should be kept in mind that the Fund suffered from an erosion of credibility attributed in some quarters not only to weaknesses in communication but also to policy mistakes. This broader characterization of the problem serves to underscore the importance of strengthening the Fund's core activities.

At the same time, the Locke study emphasizes the need to improve the Fund's influence in the environment where relevant matters are considered. There can be no dispute that effectiveness on this front is important, provided that the universal character of the Fund is not diluted as a result of this incursion. Like Mr. Esdar, we welcome the increased attention given by the staff and management to parliamentarians from an increasingly broader cross-section of the membership, and hope that future initiatives of member countries of this type, aimed at clarifying the role of the Fund and the relationship with the member, will continue to be privileged.

Mr. Dawson, the new Director of EXR, has the advantage of knowing the Fund well but still has a big challenge ahead of him to continue to professionalize and improve the Fund's public relations; to enhance the Fund's contacts with the media; to build-up the Fund's relations with legislatures; to broaden the Fund's outreach and improve relations with civil society. The additional complication is that all this has to be done within the general call for budgetary restraint that emerged from last Wednesday's staff planning discussion.

We basically endorse the plan of action. We find it difficult, however, to conclude that the significant number of staff assigned to EXR in recent years amounted to a neglect of these activities or that the level of identified staffing needs for EXR in the short and medium terms justify the trade-off in enhanced technical assistance, surveillance, or financial sector activities. On the basis of the available information, we do not feel comfortable with the level of the staffing increase requested for 2001 and cannot support medium-term requirements for EXR set out in piecemeal fashion. We are, nevertheless, prepared to go along with the consensus regarding the number of new staff to be assigned to EXR in 2001.

More specifically on some elements of the plan, the building of relations with the private financial sector, "especially institutions active in emerging market countries", requires greater specification of what should be avoided, like privileged relationships and situations of asymmetrical information. I welcome, in this regard, Mr. Dawson's clarification regarding the broader outreach envisaged for this activity.

Additionally, we welcome the increasing use of the web site, bi-weekly press briefings, granting of interviews, opinion articles, and the ever-more frequent resort to regular video teleconferencing, as promising and cost-effective vehicles to broaden the Fund's outreach. Similarly, like Messrs. Bernes and Esdar, we would underscore the need for more publications and activities undertaken in non-English languages to ensure that the drive to improve transparency and the Fund's image will, in fact, be meaningful for the intended wider audience.

In any event, we consider it indispensable that EXR activities in member countries should be coordinated with the Office of the Executive Director representing that country and, when desirable, with the national authorities. When it comes to country-specific information, we should keep in mind that even an optimal Fund communications policy cannot, and should not, attempt to substitute for the authorities' own responsibility when it comes to disseminating views regarding country-specific policies.

Regarding the strategy for promoting the Fund more effectively, overall we tend to share the general view expressed by Mr. Oyarzabál in his statement, that it would benefit from greater articulation. It is to be hoped that the paper to be prepared for Board discussion will address more directly what the Fund needs to do in this area and how to bring it about. In that context it should look at thematic approach advanced by Mr. Portugal and bring in the notion of selectivity for dealing with NGOs raised by Mr. Shaalan. In passing, I should note that a recent article appearing in the Argentine press on NGOs mentions that in Argentina alone some 100 thousand entities are registered. In addition, when it comes to the modality to disseminate country-specific information, rigid prescriptions should be avoided, keeping in mind the differing degrees of familiarity with Fund activities across the membership, as well as the resource constraints that prevail. Finally, we have sympathy for the commentary advanced by Messrs. Yakusha and Kapteyn in their statement and hope that suggestions can be worked into the upcoming proposal for the Fund's communication policy strategy in a manner that ensures that the most value is returned for expenditure.

Mr. Prader made the following statement:

Like others, we welcome this somewhat overdue paper on the Fund's new external communications strategy, which will enable us to have a discussion about the Fund's resource request. We recognize there is both a demand and a need to continue to expand the Fund's current conservative approach to external communications. The studies that have been carried out and presented to us by a number of consultants are quite convincing. Nevertheless, the finding that the Fund has become the least popular among the major international organizations is quite surprising to us. We have a very high opinion of the Fund staff and cannot quite believe that the general public does not see it that way.

It is also clear that the changes that have taken place in information technology correspond to changes in the Fund's external relations, policies, and practices. The explosion in the number of nongovernmental organizations presents the Fund with challenges that are impressive and almost insurmountable.

We appreciate that the External Relations Department is approaching this task with a positive attitude. The Director of EXR is the right person to lead this effort, and he has already achieved a great deal. At the same time, we should not lose sight of the limitations of any imaginable public relations effort. A particular constraint is that some or many member governments use the Fund deliberately as a convenient scapegoat to explain problems that actually exist at the domestic or international level.

The Fund should focus on a simple message, such as the Fund is "effective, fair, and responsive." Although this message has been well-received, the question remains whether this can fully convey the reality of the Fund's task. It may well be that being unpopular is part of the Fund's job, even though the Fund tries to project the idea that it is not a policeman but a modern social worker.

I am open-minded concerning requests by External Relations, but we have to keep in mind that the Fund's budget is on an explosive growth path. There is a need for expenditure restraint; we cannot rely on crisis countries to pay the cost of running the Fund. As a former Executive Director for the U.S., the Director of EXR will better understand such concerns.

I recognize both that the External Relations Department is facing an uphill battle, and that the growth rate of EXR staff has lagged behind that of area departments and that of the Fund as a whole. But before committing myself to specific numbers, I would like to have assurances that newly recruited staff will be real professionals and not just economists or other Fund staff members. This statement implies skepticism about some Directors' demands that redeployment will be a panacea to meet the demands of EXR.

Finally, one of the most effective external communication moves the Fund could make would be the early announcement of a strong, respected, effective, fair, and responsive new Managing Director.

Mr. Mirakhor made the following statement:

First, I would like to thank the Director of EXR for his comprehensive report and for his additional remarks this morning. I would first like to make a personal comment that I was delighted when I first heard that the Director of EXR had agreed to join us. Those of us privileged to serve with him on the Board in his previous capacity, developed a high degree of respect for his honesty, integrity, and diplomatic skills. I have no doubt that he will be among the legacies left behind by the Managing Director. I also thank him for his effective press briefings, and in particular for occasional references to the Board in these briefings. It may be that slowly but surely he will drive home the point to the press and the public that this institution has an Executive Board.

Mr. Esdar raised the issue of involvement with legislatures, which was supported by Mr. Wei and alluded to by Mr. Zoccali, suggesting that our work with legislatures should be limited to dealing indirectly with the authorities and their legislators. If our recent experience is any indication, it would be naive to assume that when legislators consider themselves independent of Executive Directors we can trust these same legislators to invest the time and effort required to explain the Fund and its policies. Legislatures have a major role in forming public opinion, and we have to be conscious not to ignore that. The Staff report has a very perceptive point in strategically targeting the U.S. Congress. For better or worse, the U.S. Congress is very important to this institution—not that others are not. We have to realize the United States is a major shareholder of this institution. We are located in Washington and highly visible here, and Washington is the center of public opinion. It is also an image-making factory, so we have to be cognizant of this. That does not mean that we should ignore or even downplay the role we have to play with the rest of the world's legislatures. It also does not mean that we have to abrogate our own responsibilities to explain Fund policies to our legislatures.

I also want to make a point to suggest that when we need to explain ourselves to the U.S. Congress or other legislatures, it does not mean that attempts are being made to influence these legislatures. We have an obligation under Article VIII, Section 5(c) to ensure that influence is not one-sided. Each member of the Fund is obligated to restrain from any attempt to influence the work of this institution or its universality. While we have to make a clear

> delineation between informing legislatures and attempting to influence them, we also have to expect and ensure that we are treated in a like manner.
>
> Let me turn to the resource needs of the Fund's external communications. I was prepared to support the Director of EXR's initial request, particularly after I had discussions on this matter with him. His view was that even if the job could be done with the initial request, it still would fall short of what is required. If the job is going to be done properly, the initial request will prove to be inadequate. I am cognizant of the reluctance of Directors to allow for the full number of staff requests. I thank Mr. Bernes for suggesting a compromise. The Board will look more favorably next year on the decision to provide the Director of EXR the resources he will need to meet the daunting challenge of making up in relatively short order 50 years of neglecting the importance of external communications.

The Acting Chairman noted that Mr. Bernes had also raised the issue of including a communications issues section in the staff reports, and that he supported the idea. It was important that Directors discuss the matter.

Ms. Lissakers said that the U.S. authorities were grateful for the briefings Congress had received, which were making a difference. Nonetheless, the manner in which those efforts were presented in the staff report made it sound as if there were a subdepartment of EXR devoted strictly to taking care of the U.S. Congress. That was not the case, and if it were, it would not be acceptable. In the coming years, the Fund would be held more accountable to legislatures around the world. Increasingly, other legislatures would begin to want more information about the Fund from Directors and from the staff. It would be a challenge for the Fund to determine how to handle this phenomenon, which from a democratic standpoint, was a healthy one.

Mr. Mirakhor commented that the sovereignty of the Fund meant that it should be free from undue influences as stated in the Articles of Agreement. It was unfortunate that the Fund went to the U.S. Congress to ask for more resources. The Fund still had to contend with the set of requirements that Congress had imposed. It was important that the Fund educate and inform legislative bodies about Fund policies and constraints. But, there was no benefit in pursuing a policy of trying to influence legislatures because legislatures would undoubtedly attempt to influence the Fund in return.

Ms. Lissakers remarked that it was not wrong or unfortunate that the Fund went to legislatures for resources. Resources came from shareholder countries, which meant from the citizens of the individual member countries. When the Fund's budget was discussed, the Fund had to keep legislatures and their citizens in mind because resource allocation would have to be defended in the U.S. Congress and other legislatures. The need to go to legislatures to ask for financial resources was the vehicle for the legislatures to reaffirm their countries' commitment to the Fund. For example, critics of the Fund have said that with regard to Russia, the Fund bypassed the Duma along with other legislatures. Yet, legislatures had an opportunity to signal whether or not they broadly support the Fund through the quota votes that have gone to most legislatures. Those votes were a reaffirmation of national support for the Fund.

Mr. Wei, in agreement with Mr. Mirakhor, expressed concern that the U.S. legislature was singled out for special treatment. The United States was important to the Fund because of its economic contribution. But if European countries were placed together, they would have a larger share of power than the United States. Financial assistance from Japan was also formidable, and it was not clear what was the appropriate manner in which to proceed with respect to legislatures of those countries. Directors should be very careful in considering the staff's proposal on this point.

Mr. Mirakhor remarked that it was clear that European countries were not unified. The suggestion that efforts to concentrate on the U.S. Congress should stop did not mean that efforts to educate Congress about the Fund should cease. Recent comments by congressmen indicated that perhaps there was a general level of ignorance of the Fund and its functions. Similar comments had not been heard from the Japanese or German legislatures, or from the rest of the Fund's membership. Similar comments might be made, but they were not reflected in the press, while the U.S. Congress' positions were.

Mr. Esdar thanked Mr. Mirakhor and Mr. Wei for their encouraging remarks about Europe, and said he would report them to his authorities. On the issue of the relation between the Fund and legislatures, it should be clear that, in line with Ms. Lissakers' point, the Fund must consider legislatures because they have an obligation to check the Fund's budgetary process. That did not mean that the Fund should support everything legislatures suggest, or appeal to legislatures to override decisions made by the authorities.

The Acting Chairman said that in many countries the Fund could rely on governments to explain Fund policies and concerns. In the case of the British, the House of Commons Committee was charged with the responsibility to come and talk with the Fund. In the United States, the Fund did not formally testify to Congress, but did give testimony to congressional commissions along with speaking to Congress in informal ways. It would be unfortunate if the Fund had to make similar efforts for other countries.

Mr. Prader stated that he agreed with Mr. Esdar's position on the relationship between the Fund and legislatures. In response to Mr. Mirakhor's comments on European unity, outsiders were always surprised about the length of time it took to make decisions and to reach unity in Europe. Nonetheless, there was more unity among Europeans at present than at any time in the recent past, and eventually there would be total unity.

Mr. Collins remarked that there were now two U.K. parliamentary committees that were charged with communicating with the Fund, and they had both been to Washington, D.C. recently. Also, for the first time, Mr. Pickford had to give evidence in London to both of those committees.

Mr. Cippà made the following statement:

I think we all agree that we have come a long way from what was described in the last staff report as a “restrained, scholarly and conservative” approach that characterized the Fund’s past external communications policy. We consider external communications as an important element in our overall endeavor to increase the transparency of our institution. The efficiency of our institution not only depends on the quality of its work but also on how the public perceives this work.

I would like to take this opportunity to thank Mr. Dawson and his team for the significant improvements that have taken place since last summer in the area of media relations. The comprehensive website, the regular press briefings and the increasing number of newspaper articles by Fund management and the staff are just a few examples. While most of the measures taken so far certainly go in the right direction, in my view we are still lacking what the Edelman/Wirthlin study called “a communications strategy”. Such a strategy should contain guidelines with regard to the audience to be addressed, the instruments at hand (publications, press contacts etc.), and the image the Fund wants to propagate of itself.

Today’s paper presents us with a long list of ways in which our external communications efforts should be increased. I agree with Mr. Yakusha and Mr. Kapteyn, that the link between the external studies performed last year and this paper is not satisfactory. It is unclear to me according to what criteria the currently envisaged measures were chosen and how the resource needs were derived. Let us not forget that EXR was already using 69 staff members in 1991, a time in which external communications was still on the back burner. Has a redeployment of resources taken place? Apparently yes, and also quite successfully. Is there scope for further action?

Mr. Chairman, I share many of the points raised by Mr. Bernes and Mr. Esdar. Therefore, I will comment only on two points, for emphasis.

An important point made in the Edelman/Wirthlin study is that an effective communications policy will depend not only on changes within EXR, but even more crucially on the appropriate involvement of the staff, management and members of the Executive Board. Therefore, efforts to train these actors in their interaction with the public, particularly with the media are very important. For example, this would allow us to better utilize our net of resident representatives, the mission chiefs and the various regional institutes to implement our strategy in the field. In my view, EXR should avoid getting directly involved in fieldwork. Regarding media training in general, I would be interested to know if the training would be provided in-house or if it is out-sourced.

Training would also improve the senior staff's capacity to interact with the various interest groups such as NGOs and national legislators. Regarding the latter group, like Messrs. Yakusha and Kapteyn, I was surprised by the weight that seemed to be attributed to lobbying members of the U.S. Congress. I am somewhat reassured by the initial remarks by Mr. Dawson that we will add less than one staff member for that purpose. Still, I disagree with the implied view that the Fund should lobby for itself in national parliaments.

First, I believe that it is not the job of any multilateral organization to proactively propagate its issues in national legislatures. Lobbying parliaments is primarily a task of national authorities. This is not to say that Fund management should not, for example, be available for discussions and hearings with parliaments, as was the case in the past.

Second, it is obvious from the staff paper that the intended lobbying would very much concentrate on the U.S. Congress. While this parliament is certainly very important to the Fund, I am not sure that this special attention would be well received by the parliaments in other member countries. Possible contagion effects might also be detrimental. It is not to exclude that the reason why other parliaments do not ask at present to be briefed like the U.S. congress, is because they do not perceive this as feasible. All in all, and given our resource constraints, the IMF should not actively expand its activities in this direction.

Turning to the relations with the private financial sector, I welcome the intention to increase communication with the financial centers outside the United States. But, as said by others, informational exchange with the private financial sector should take place on the level of the staff and management since market participants are most likely to prefer communicating with technical experts rather than with communication specialists.

Finally, on the issue of resource needs. In view of the importance we attach to external communications, we would clearly favor an increase of the staff resources for EXR. However, in our recent budget discussion we argued for overall limit on net increase of staff resources for 2001, including EXR, given the multitude of new initiatives and the difficulty in determining the various resource implications. This would have given management some flexibility in resource distribution. I continue to believe that this is the right approach, and I continue to believe that a number around 105 is appropriate.

Mr. Collins made the following statement:

I am grateful for the paper from the staff, but regret that Directors were not able to talk about the subject before the budget discussion. The notion that the Fund has a public relations problem is nothing new. On the basis of files dating to 1981, much of the discussion then is being repeated today. I will remind the staff that the Managing Director in the early eighties wrote a speech called Ten Common Misconceptions about the Fund, which turned into a pamphlet which could still be issued by EXR today. Nonetheless, it is fair to say that the current steps which have been taken to address the problems of external relations are the most concerted in the Fund's history, at least in terms of analyzing the nature of the problem and considering solutions.

The Fund is more transparent than ever before, so the External Relations Department has much more raw material with which to make a contribution. We should recognize that notable achievements have already been made, and I particularly point to the website which does get universal high praise. There is a question as to whether there is a sufficiently consistent approach to promoting the website at every opportunity. In any event, I agree with those Directors who argue that the staff paper does not of itself set out a coherent communications strategy, so this should in many ways be regarded only as a preliminary discussion.

I will suggest two or three points on what is needed to develop a coherent strategy. First, I observe that the motto suggested for the Fund of "effective, responsive, and fair" might serve as a description of how the Fund does what it does. But it does not say what the Fund does, and that raises the question of whether there should be a mission statement. I would not want to invest too much faith in such a statement, but it might help in branding the Fund in a more positive manner, and ought to help in setting the objectives of the organization in a coherent way.

Second, on the questions of how proactive or reactive the Fund should be, it is probably inappropriate for the Fund to be too aggressive in attempts to preempt criticism, other than disseminating honest information about what it is doing.

Third, the Edelman survey found that people who were educated about the Fund usually had a more positive assessment of what it is. Yet the conclusion that more education is needed does not address the question of what that education might include or entail. School children ought to learn about the Fund in the same manner in which they learn about other institutions.

I too have been uncomfortable with the manner in which the paper presents the work directed toward the U.S. Congress. The issue is more perception rather than substance. I have no doubt that the U.S. Congress is the most important legislative body that the Fund must address for all the reasons discussed. It is not irrelevant that we are here upon their doorstep; indeed, it is highly relevant. Yet, in terms of any public presentation—if there is any public presentation—the Fund's strategy should be defined in a more subtle manner than what was said in the paper.

On the relations with the private financial sector, there should be great emphasis on the collaborative role of departments within the Fund and the relevant private financial markets. The responsibility for this job should lie with mission chiefs and the heads of departments.

I broadly agree with what is presented in the paper on recommendations for improved media relations, and the Director of EXR has done a good job so far as a spokesperson. In addition to the role as spokesperson, he is charged with the roles of liaison to both Wall Street and Congress. It may neither be appropriate nor feasible to have all three jobs mixed together. I infer from the paper that the spokesperson role is now his predominant responsibility, while the other roles will be within the department and elsewhere. Nonetheless, I would be interested to hear his view on this subject.

On the demand for publications, page eight of the paper identifies weaknesses with the present strategy, and notes a need to move from a supply-driven to a demand-driven publication approach. Nonetheless, the paper does not elaborate on how this might be achieved. Do we keep a consistent list of inquiries so that we can actually judge what the market wants? Should we start charging for hard copies, given the wide availability of information on the web as soon as possible?

It is clear that there are too many NGOs to engage feasibly with, but that does not mean the Fund should engage with none. The image of the Fund has improved notably through implementation of the PRGF which has as much to do with substance as it does with public relations reasons which that have been facilitated by NGOs.

The External Relations Department is bigger than you would typically find in a large British government department, though it must be remembered that its constituency is the world and not just one country in a sense. It would seem that there should be scope for redeployment of resources within the Fund. I could go along with a figure of about seven additional staff, which would bring us to an increase of 105 staff in total. But it is probably premature to come to a conclusion until we look at a more precise strategy.

My final point is to agree with Mr. Esdar on the need to diminish the use of acronyms in Fund documents, and I hope that the Director of EXR will facilitate this process.

Mr. Yanase made the following statement:

We strongly support strengthening of external communication activities by the Fund. During the Asian crisis, the Fund's efforts were too little and too late. It seriously undermined our ability in performing our tasks, and held potential damage to the Fund's morale. The consultants' report also showed clearly that substantial efforts must be made in this area. In addition, we believe our efforts to increase the transparency and accountability of this institution must go hand in hand with improvement in our public relations to achieve its intended purpose.

Overall, I support the initial action plan proposed by the staff. We also commend significant efforts made to date by management and the staff to improve our public relations.

However, I share the dissatisfaction expressed by some Directors that the staff proposal for today's discussion is a rather limited one, and does not address many important issues and ideas raised by outside consultants. We would also like to know details of outreach activities to civil societies or to the private financial sector, which require careful handling, as was voiced by other speakers. I look forward to the paper which will be presented to the Board for the discussion this summer and expect it to include a more complete description of reactions to the consultants' findings and recommendations, and experiences with the initial implementation of the proposed action plan.

Regarding communication with parliaments, I share concerns expressed by other Directors, and I particularly associate myself with Mr. Cippa's concern of a proliferation of activities in connection with other legislative bodies.

Concerning resource implication, we agree a certain increase in staff resources is necessary to strengthen external communications. By nature, these are very labor-intensive activities. We are prepared to accept the staff proposal of 17 more staff positions for 2001, given the Board has determined the increase in other areas to be relatively modest. However, like Mr. Shaalan, we can go along with a consensus, if one emerges. In allocating resources, we ask the staff to consider the important role played by regional offices in Asia and Europe. Time differences require these offices to play a vital part in the Fund's external communication in a world that operates around the clock, and the communication function of those offices must also be strengthened.

Mr. Bauche made the following statement:

I welcome this opportunity to discuss the Fund's external communications action plan. Recent discussions have shown that we need to link closely our initiatives with the corresponding needs of the staff.

Several speakers have mentioned that even with the best communications strategy, it would be hard to reduce the Fund's level of unpopularity. It can be argued that the Fund's general purposes are served by standing behind unpopular policy reforms allowing authorities room for maneuver while the Fund serves as the scapegoat.

I very much appreciate the press briefings conducted since last October by the new Director of EXR. Transparency of the Fund is important, but pedagogy is equally important. I would say that explaining to the public what the Fund does is as important as what it does.

The Director of EXR's skills could also be useful to increase training for those staff with frequent outside contacts. Communication is not something that should be concentrated in central Fund units, but something that should emanate through the whole staff and the Executive Board. Like Mr. Collins, I note with interest the fifth paragraph on page nine of the staff paper which says that the Executive Board will be asked to commit itself to a general strategy. Nonetheless, Directors are also called upon to take responsibility for promoting the Fund more effectively within their own countries. Directors will want to know what exactly the Director of EXR expects from them.

The Fund's web site is the best source of our external communication because it gives the highest return for the smallest amount of resources. I am prepared to support the initial proposal for additional resources to hire more staff for EXR, but I understand that there could be a consensus on a somewhat lower number.

Mr. Barro Chambrier made the following statement:

The paper prepared by the staff for today's discussion makes a compelling point as to why the Fund needs to strengthen its communication capabilities and skills. Indeed, member countries and the public at large require international organizations to be more transparent, more accountable, and more efficient in delivering their services.

However, although we understand the staff's request for more resources allocated to external communication, we have to admit that the figure on "Job Favorability of World Organizations" does not constitute a compelling argument. Indeed, purposes, processes, and the impacts of those organizations are very different.

Turning now to specific areas where the Fund needs to enhance its communication skills, we see some critical domains.

Good communication begins at home. It is our view that good internal communication is a prerequisite for an efficient external communication. In order to faithfully and effectively convey the Fund's message to the outside, the Fund's managers and the staff need to communicate better. Moreover, the so-called culture and uniqueness of the Fund should not constitute an excuse for not accepting criticism and new ideas.

With regard to dialogue with member countries in certain cases, it is critical to fill the communication gap between the authorities of some countries and this institution. It is our view that the Fund does not deserve the bad image mentioned in the staff paper. However, we have to regrettably admit that the Fund's programs are sometimes viewed as "imposed," with little say allowed to recipient countries. Here, the new emphasis put by the Fund on ownership is particularly timely. Furthermore, the Fund's economists in contact with government authorities should be able to explain policies in a manner which is convincing to authorities. To that end, we believe that the Fund's resident representatives and regional offices have a critical role to play.

Concerning the information provided to the larger public, we would like to insist on the importance of the annual report. We consider it as a medium in its own right. Indeed, it exhibits the policies, activities and results of the Fund. It is our view that the Annual Report of the Fund can be made friendlier by not just displaying numbers and tables. In that respect, we suggest an effort to redesign the Annual Report. Also, like Mr. Bernes, I believe that the Fund needs to publish in languages other than English.

Regarding the Fund's communication with the media, we regret that there is only one media relations officer covering Africa. This is clearly an area where the External Relations Department should devote more attention and means.

Finally, concerning the resources needed to enhance the Fund's external communication, we can go along with the consensus.

Mr. Lehmussaari made the following statement:

There is no question that the Funds external communications are a necessary and important part of the Fund's operations. Recent situations and a changed operating environment, in combination with the poor public image of the Fund, have created new demands on the External Relations Department. I have no doubt that this department is doing a commendable job under intense pressure and difficult circumstances.

However, I am not convinced that the solution to the Fund's communications problems will be found just by adding more people to EXR.

Moreover, within given resource constraints, it is difficult to find room for a major expansion. I believe that there is much room to improve the image problem by utilizing the current staff. Nonetheless, I could support some additional resources for enhanced transparency through web site and media services.

Turning to the lack of effectiveness in external relations, I agree with the consultants that there are many flaws in the Fund's communications, and I agree with the notion that the Fund should try to devise clearer and simpler messages. However, I am not as convinced that the alleged bad image can be contributed only to poor communications. The work of the Fund is by default simply less popular with the public than that of the Red Cross or the World Bank.

That said, I am not advocating that we should not try to improve the Fund's image, but we may have to employ more modest and longer-term strategies. Much more can be done in terms of empowering mission chiefs and resident representatives with communication skills that can be employed in the field. Too often, mission chiefs and resident representatives do not have a clear and simple message to deliver, and too often their response to the media and the public is reactive. Management should focus more on making communications an active part of an economist's job, rather than attempt to cover all bases from an overarching External Relations Department. Meanwhile, the External Relations Department should play an active role in devising strategies and empowering those in the field. Management ought to support such efforts fully.

More generally, I share many of the views presented in Mr. Yakusha's and Mr. Kapteyn's statement. In particular, their point with regard to reaching the private sector is well taken.

I also share the skepticism expressed by Mr. Esdar with respect to increasing the number of publications.

Finally, I would like to stress that I am not in a position to determine the right amount of staff to add to EXR. Although, I am definitely leaning towards a much smaller number than that proposed by the staff. If there is a consensus around a reasonable number, I can go along with it in good faith. However, as Mr. Bauche noted, it is difficult to see what this consensus number is.

Mr. Lushin made the following statement:

First, I would like to welcome the progress achieved by the staff in improving the Fund's external communications over the recent period of time. Since our previous discussion on this matter, several steps have been undertaken by the External Relations Department, including further development of the Fund's external website which now proves to be one of the major tools for the Fund's public relations. The volume of publicly available information on the Fund's policies and relations with member countries has increased substantially as a result of a strong presumption in favor of transparency. Communications with the media have also improved, mainly because of the introduction of a spokesperson and the practice of regular briefings to the media. I am convinced that all these achievements are very conducive for strengthening and sharpening the voice of the Fund.

The surveys undertaken by the external consultants highlighted several weaknesses in the Fund's external communications and provided useful recommendations on how to improve the situation. I can hardly disagree with the general thrust of these recommendations. I broadly agree with the general framework for the strengthening of external communications policies as suggested in the staff paper. Let me now turn to some specific issues.

I fully concur that the Fund should take a more proactive position in explaining its work to a wide range of public. The purpose is not only to defend the Fund from criticism, which is unavoidable because issues the Fund often must address, but to improve understanding of the Fund's activities necessary to obtain respect and credibility.

The building of relations with the private financial sector is also crucial. The Fund continues its efforts to involve the private sector in the prevention and resolution of financial crises. In this context it is important to strengthen the Fund's image as a credible and powerful financial institution.

Communications with the media should be enhanced further. The developing of media guidelines for the staff may be helpful as well as an intensified media training program for resident representatives and mission chiefs. Moreover, I believe that the resident representatives should be more involved in the communication with media and the general public in the host countries.

Although much progress has already been achieved, further work needs to be done to develop the Fund's external website.

I welcome improved collaboration of the External Relations Department with other departments and units across the Fund, including regional offices. An adequate sharing of information on a timely basis, as well as the development of the common strategy for external communications, will make an important contribution to the strengthening of the Fund's external communications in general.

Finally, on additional staff resources, I will speak only about the 2001. First, I think that the three positions requested for external communications work related to the poverty reduction strategy should be incorporated within the staff increase for the PRGF and enhanced HIPC Initiative, which has already been approved. Second, for the remaining 14 requested positions, in view of a tight budget situation, I suggest to apply a coefficient of consolidation, which was in place by moving from budget Option 1 to Option 2a. In this case scenario 10 new staff would be added to EXR in addition to the staff increase for the 2001, resulting in 108 new people. This quantity is not far away from the figure of 105, suggested by Mr. Bernes and supported by a number of other Directors.

Mr. Kelkar made the following statement:

Let me thank the Director of EXR and his colleagues for a comprehensive paper. The Fund's image has been improving, but the product the Fund produces has also been improving. Although, we may have put the worst behind us, I am willing to go along with the minimum of all the numbers proposed for an increase in the staff of EXR.

On the interaction between the Fund and legislatures, there is no escape from greater interaction with the legislatures and the Fund. I have no solutions as to what exactly should be done, but more activity will be required, and perhaps it is appropriate to prepare. I agree that attention and responsibility for communications should be paid by Board members with respect to their member countries. However, Fund mission leaders or Fund representatives should not get involved in the domestic politics of a particular country. Such involvement may be viewed as interference in the domestic processes.

There should be a regional emphasis in the exercise of external relations. I reiterate my earlier suggestion that perhaps one staff member for the whole of Africa is inadequate, and that regional offices would serve better in communicating the policies and results of our major new initiative, the PRGF.

Mr. Schlitzer made the following statement:

The Fund's external communications are of tremendous importance. As other Directors, we would like to commend the Director of EXR and his staff for the significant improvements in our communication policy that have been accomplished in a very short period of time. Let me note, however, that efforts to improve in this regard should be a Fund-wide exercise and not just that of the External Relations Department.

I must say that I share the desire expressed by other Directors to have a more comprehensive paper outlining an external relations strategy for the future, and in particular how the staff intends to respond to the Edelman report. The paper should also address the issue of how external relations is going to be reorganized.

On the delicate issue of resources, the External Relations Department is not small. It consists of 80 people. It was granted a 16 percent increase for the current financial year. On this premise, along with a shortage of information, I cannot support the request for an additional 14 positions. Though in light of the attention we give to the Fund's external communications policy, I can go along with an increase of ten positions.

Mr. Djaafara made the following statement:

For the record, we support the plan to strengthen the External Communications Department as suggested by Mr. Bernes, though we emphasize the need to pay attention to budget constraints. We join other Directors in encouraging management to privatize the external relations strategy and to redeploy the EXR staff.

Ms. Lissakers made the following statement:

In addition to the well-known Meltzer Commission, there is an Advisory Commission to the Treasury, mandated by the U.S. Congress, which includes people from business, labor, NGOs and finance. I attended a meeting of this group yesterday, and the CEO of a large agricultural firm who is supportive of the Fund and, indeed, an internationalist, said that if he had been receiving press as bad as the Fund had received over the last few years, he would have fired the head of public relations and created a whole new operation. Though we have not fired anyone, as far as I know, I assured him we were operating on similar lines. He then added that the Fund was receiving better press as of late.

I would add that this CEO has his own internal public relations operation. He was frustrated with workers who were not conscious of the value and importance to their livelihoods of exports to foreign markets. Consequently, he started including in their paycheck envelope a note saying that 38 percent of their paycheck came from exports of the company. Similar efforts in other firms would help build public support for the Fund in the future.

The regular press conferences constitute the most valuable and commendable steps taken by EXR. It brings to mind a conversation I had some years ago with the international division head of a medium-sized bank. He stated that his bank was in the euro market. They borrowed EU100 million every night in the euro market. I asked why. He responded that the reason was because they did not need it. They would borrow it and put it back the next morning, so when the time came that they did need to borrow, nobody would take any notice. It would be routine. This is the same value of having a weekly press conference.

Though it takes a lot of time for management, I hope that we will continue to have high-level management participation in press conferences. It is invaluable that the world become accustomed to the Fund, so that when there is bad news—and there certainly will be bad news—it does not come as a surprise.

I would also note that the press remains probably one of the more efficient means of dissemination. They may not be infallible, but they are an effective and efficient means of getting a story out, which is not to say that other more direct communications with various audiences is not also extremely valuable and certainly something that we support.

On the question of numbers and additions to the staff, one way to solve the budget problem would be, perhaps, for all the members of the OECD to transfer the number of extraordinary resources that are being devoted to their operation. In the paper it says in a footnote that they have 120 people devoted to public relations for the OECD. This is excessive, and maybe our members of the OECD should devote a number of those resources to the Fund which would seem to have a more legitimate need for additional staff.

The ten additional staff members suggested by Mr. Dawson seems about right for a very ambitious undertaking. Although, given the total staffing increases that were discussed the other day which I think are too high, it would have been preferable to include the additional ten in a lower overall increase.

I reiterate that we should be mindful of the price tag that comes with these staffing increases, which Mr. Prader quite usefully highlighted today. A 37 percent nominal increase in the budget over three years is a lot even acknowledging the additional demands that have been placed on this institution.

Mr. Prader asked for a reassurance concerning the envisaged qualifications requirements for the additional staff to be hired, and clarification on how the hiring process would proceed.

The Director of the External Relations Department made the following statement:

First, while the numbers mentioned of 10, 14, and 17 additional staff seem large, I want to reiterate that EXR's role within the Fund is consistent with the word modesty. We understand our job is to help the Fund as a whole, so we do not view ourselves as a department that has a life of its own. It is in this context that we look at our effort.

With regard to cooperation with other departments, we have reached understandings with basically every department. Area departments vary from case to case, but departments all share fairly extensive information. It is already the case that we give guidance to resident representatives as well as to mission chiefs based on information from area departments that passes through EXR. In this regard, we will report back to Directors on any recommendations voiced at the Board or in the Edelman report that have not already been implemented.

Regarding redeployment issues and the manner in which new staff will be hired, media relations staff will be hired from outside the Fund, and will be hired for those regions which are undercovered. For positions associated with the website, it is entirely possible that people will be sourced internally because of the level of expertise necessary.

One of the difficulties within EXR and the relations with the rest of the Fund is that there are almost no economists on the EXR staff. The Deputy Director is no longer counted as an economist, which leaves us only with the speech writer. This is not adequate. We are in the market for a couple of economists to come into the department. Preferably, one would come from outside who used to be with the Fund. It is quite likely that the other one would be recruited from inside the Fund. Obtaining the best and the brightest is certainly part of our agenda.

On the issue of the style of language in the Fund, there is a conflict between some Directors' comments and the resource situation. We clearly want to simplify language. Much of what is published at this point is edited by EXR, and we get to a document relatively late in the entire process from its creation to its dissemination. We do not need to increase massively the staff to be able to rewrite every document we need to work on. It is mentioned in the paper that departments need a style guide to write in a more user-friendly fashion, which would save time and resources.

On the manner in which I spend my time in attempts to perform different duties, much of my time has been spent on media issues and Capitol Hill issues. But the amount of time spent will decrease once the initial round of get-acquainted calls has taken place. On private sector involvement, this has been an area of particular interest and emphasis because I was working on the private-sector side of exactly the same issue at Merrill Lynch prior to coming to EXR. Part of my role in increasing private-sector contacts will be to serve as an advisor to PDR and management on how to approach private financial institutions, particularly non-U.S. institutions. In my previous capacity, I served on a number of steering committees, and in some sense of the word it is that expertise that Fund is trying to build upon. This private sector contact requires a very modest amount of support or resources. It is an attempt to utilize my own network of contacts on behalf of the Fund.

I take note of Directors' comments on this paper that it may not be the overall strategy people were hoping for. The paper was put together on fairly short notice because of the budget issue, and we are prepared, if Directors wish, to come back with a more complete strategy, although as some Directors indicated, this clearly would require a broader and more defined view of the Fund. I understand Directors have been discussing that issue in their own seminar.

Ms. Lissakers made the comment that the press conference is a forum for getting views together. It has been suggested that media relations are costly and have low marginal return. This is not the case. There is a high return by bringing different views together, and a high return in providing Directors with more information. We will continue to find more ways to provide Directors with more information in a rapid manner. We are also considering appropriate public forums where Directors could address issues. We are considering a seminar or two with participation of the Board, members of the press, NGOs, and congressional staffers. It would be appropriate to have one or two Directors to participate in those sorts of seminars.

On parliaments, there is a general increase in interest by parliaments in the work of the Fund. Directors will have to determine in what manner they wish to deal with this increased interest.

Our concept of external relations is very different from that at the World Bank. They of course have a much larger staff, and have people placed within area departments and resident offices. Our role is a support role, and we view ourselves as far more a headquarter-based operation. Our travel is relatively modest. Our media relations staff do travel in support of management and on occasion hold regional press seminars. We do travel in support of research and do presentations—for example, on the World Economic Outlook. In the future, there will be more EXR staff in the public environment, but there will be very few. You will not see a drastic change of the level of activity in terms of outside presentations by EXR. Outside presentations are primarily the responsibility of area departments, regional representatives, and functional departments.

On publications, we are certainly trying to develop ways to receive feedback to make the process more demand-driven. The web has become the medium of dissemination in many respects, yet it is not clear that it can serve as a signaling device for demand, given that people can download documents. At the moment we still have more demand for publications than we can fill, and we are attempting to focus on those publications that are of a more general interest. We hear clearly the need and desire for publications written in languages other than English, both in the case of paper publications as well as those on the web site.

On NGOs, there was unease throughout the Board on how to determine which NGOs to deal with and under what circumstances, the Acting Chairman observed. At some point, the Fund would need to review this matter. But, at present, the Fund should engage with NGOs. They more or less had to be considered, and presumably Directors and the staff would use common sense in deciding with whom to speak .

The Acting Chairman made the following concluding remarks:

Executive Directors welcomed the opportunity to follow up on the Executive Board's discussion in July 1998 of the Fund's external communications policy in the context of the Fund's medium-term budget for FY2001—FY2003. They commended the External Relations Department (EXR) for the significant improvements in the Fund's communications policy since the last Board discussion. Directors agreed on the need to strengthen further the Fund's external communications, and to provide resources for implementing a strengthened strategy.

Directors noted that the external assessments of the Fund's external communications in 1999 undertaken by consultants on the advice of Directors had been valuable. They viewed the findings as indicative of the challenges that the Fund must address in order to communicate more effectively with the public. Most Directors broadly concurred with the overall conclusion of the various studies that the Fund suffers external communications problems and has a less favorable public image than those of comparable international organizations, and that these factors can undermine the effectiveness of its operational work. However, they recognized that the Fund's mandate inevitably places limits on its popularity. Directors generally agreed with the consultants' findings that the Fund's external communications problems can be addressed through broader, deeper, and more proactive efforts. They also recognized that the increased openness and transparency expected by the membership of the Fund will place even greater demands on the Fund's external relations function, and require improved coordination of external communications activities within the Fund staff. Indeed, Directors underlined the need for a Fund-wide effort to improve internal communication, including an important role for the Executive Board.

Directors considered that the plan of action proposed in the Staff report reflected well the consultants' recommendations, the views of senior staff and Executive Directors obtained as feedback on the consultants' findings, and guidance from management. However, some Directors requested greater exposition about the links between the current and proposed use of resources and the consultants' recommendations. Directors welcomed many of the initiatives proposed in the plan. They regarded most of the proposed measures and actions as having the potential to contribute significantly to preserving and enhancing the credibility of the Fund, which Directors had singled out in July 1998 as the most important objective of the strategy to strengthen external communications. In particular, there was agreement on the immense public communications value of the Fund's external website, and on the need to increase the output of material for the print media and the public explaining and defending the Fund's work, and to sharpen "the voice of the Fund." Among other valuable elements of an enhanced communications strategy, Directors referred to the need for greater outreach to civil society in conjunction with the national authorities concerned, a strengthening of the Fund's publications program, engagement of member countries' legislatures in coordination with the Executive Board, and improvement of relations with the private financial sector. They also underscored that the Fund's efforts should have as broad-based and wide-ranging an outreach as possible, especially in view of its near universal membership. Directors welcomed the fact that a number of the elements of the plan have begun to be implemented using existing resources, with positive results and feedback.

In support of the need to strengthen Fund communications, and in particular the various measures proposed by EXR, Directors agreed that an additional 10 positions could be added in EXR in FY 2001.

We have taken careful note of the many useful suggestions and comments made by Directors today, including the proposal by some Directors to consider including material on communications issues in policy papers and country Staff reports. We will reflect further on these suggestions as we carry forward our efforts, and work toward strengthening a strategic approach for our external communications policies.

3. INDONESIA—EXTENDED ARRANGEMENT

The Executive Directors considered a staff paper on Indonesia's request for an Extended Arrangement in an amount equivalent to SDR 3,638.0 million (EBS/00/8, 1/20/00; Sup. 1, 1/20/00; Sup. 2, 2/1/00; and Sup. 3, 2/3/00).

The Deputy Director of the Asia and Pacific Department noted that further progress in implementing the remaining regulations for the corporate restructuring framework had been made. In particular, the mediation principles which were essential for setting deadlines to test the co-operation of debtors under the JITF had been finalized.

Mr. Harinowo made the following statement:

Since the last Executive Board Meeting on Indonesia in August 1999, the Indonesian authorities have shown considerable progress in restoring macroeconomic stability and decisively implemented the economic program under the current extended arrangement. In light of this positive development, peaceful completion of political transition and the appointment of a new government with a wide popular mandate have set the stage for a brighter prospect for the economy.

Nevertheless, the authorities are well aware that much remains to be done to expedite further progress in securing Indonesia's economic recovery. Right from the outset, the Indonesian authorities have worked closely with the Fund in developing a new economic program that is firmly grounded in the State Policy Guideline, designed to reinvigorate the economic reform agenda. The authorities have announced the new comprehensive medium-term strategy and policies for 1999/2000 and 2000 in the context of a new extended arrangement with the Fund, for which they hope to obtain the Board's support.

Macroeconomic Developments

On recent developments, a sign of recovery has become more apparent since the second quarter of 1999. Quarterly real GDP growth has been positive for the four-consecutive quarters in 1999. In the fourth quarter, real GDP is estimated to grow by 5.7 percent (y.o.y) as compared to 0.5 percent in the previous one, leading to an estimate of 0.1 percent GDP growth for the whole of 1999. The economic turnaround from deep recession to positive growth has been most dramatic, especially in the construction and manufacturing sector, being consistent with the consumption led nature of the recovery. The favorable developments have also been indicated by a positive sign from a number of leading indicators such as cement sales, vehicle production and sales, telephone subscriptions, and retail sales.

Despite interruption during the second half of 1999, due to the Bank Bali case and the prolonged political transition, macroeconomic stability has continued to improve on both domestic and external fronts. The rupiah exchange rate has been stable at around Rp 7000 per U.S. dollar during the fourth quarter of 1999.

Inflationary pressures have subsided considerably in 1999, with annual CPI inflation at end-December attaining 2.0 percent. The low inflation rate during 1999 was attributed to a restrictive monetary policy stance, supported by improvements on supply side owing to a rehabilitated distribution network and a stable exchange rate, leading to seven consecutive monthly negative inflation since March 1999. Therefore, the second and the third quarters price development showed negative inflation of 2.6 percent, and 1.9 percent consecutively, while in the fourth quarter, inflation rate reached 2.0 percent (q.o.q). The emergence of inflationary pressures in the forth quarter was mainly due to seasonal factors, such as Christmas, New Years celebration, Ramadhan, as well as increased cash demand associated with Y2K concerns. All of which lifted up consumption demand.

These favorable economic developments provided the monetary authorities with greater latitude to ease monetary conditions in order to induce lower interest rates and encourage active lending to support economic activity. Interest rates have fallen substantially to the pre-crisis levels. The one-month SBI interest rate was 11.16 percent as of January 26, 2000. The gradual yet frequent adjustments were made to ensure that the interest rate cuts were not jeopardizing the recently gained macroeconomic stability.

In order to maintain the economic stability, Bank Indonesia has firmly controlled the base money. To date, the base money target performance has remained largely on track, with the exception for December 1999. Based money moved sharply above the revised 1999/2000 path during December, owing to the cash demand associated with Y2K concerns and in anticipation of the festive season of early January 2000. Beginning in early January, both base money and NDA have begun to decline. Improved market sentiment is also reflected in the stock market. The Jakarta Stock Market Index went up from a level of 550 before the presidential elections to over 670 at the end of December 1999.

Market confidence has also been helped by the sizable turnaround in Indonesia’s external situation. The current accounts in 1999 shifted into large surplus attaining 3.5 percent of GDP, despite an uneven export performance and weaknesses in export prices. The increase in exports was due to higher oil/gas exports, while non-oil/gas exports remained largely stagnant. The lackluster performance of total non-oil/gas export has been associated with lack of financing availability, recession in a number of important market countries, and lower average export prices. Import levels continued to remain low, reflecting a slow, but accelerating, recovery. The current account surplus is developing stronger than envisaged, helping to offset a weakness in the capital account. In aggregate, the Indonesia’s balance of payments in 1999 still encountered a surplus of $3.4 billion, and thus the gross international reserve at the end of 1999 increased to $27.1 billion or equal to 6.6 months of imports.

As regards fiscal issues, consistent with the changing macroeconomic environment and the efforts to provide a fiscal stimulus to the economy, priorities were made to postpone the financing of costly investment spending and, instead, focused on financing the bank restructuring and recapitalization as well as social safety net programs to cushion the impact on the poor. The fiscal deficit for 1999/2000 is currently estimated at about 3.75 percent of GDP. This deficit has fallen below its budgeted level, principally because of development and social spending shortfalls in the first half of the year (associated with the prolonged political transition), while during this fiscal period, higher oil prices have contributed to containing the fiscal deficit. An ongoing recovery in development spending should ensure positive fiscal stimulus during the second half of the fiscal year. The financing need will be fully met by privatization receipts, assets recovery, and foreign financing.

Efforts in restructuring the banking sector have been accelerated as they continue to be the core of the economic program. The progress was envisaged in the restoration of public confidence in the national banking, recovery in liquidity condition, improved capitalization and a better prospect in profitability of banks. In the meantime, Bank Indonesia continuously strengthens its banking regulations in compliance with international standards and enhances its supervision function, including an improvement in bank supervisors' competence and integrity. Nonetheless, the Indonesian banking system is still passing through a very difficult period of restructuring, re-capitalizing and re-balancing the financial position of individual banks.

Monetary Policy for 2001

Monetary policy will continue to remain prudent to ensure that interest rate reduction will not result in renewed inflationary pressures or excessive exchange rate volatility. An indicative monetary program for 2000 has been formulated to accommodate anticipated higher growth. As confidence improves, recovery gathers pace, and foreign capital inflows resume, the authorities anticipates that a more expansionary monetary program could be justified, while keeping inflation low. Therefore, the base money is targeted to increase to about Rp 92 trillion by end-December 2000.

Fiscal Policy for 2001

In adopting the fiscal target for FY 2000, the authorities weighed carefully the balance between supporting the recovery and beginning the delicate fiscal consolidation. With recovery underway and expected to be supported by an intensification of structural reforms, the authorities adopted a conservative target for the fiscal deficit (5 percent of GDP). About half of the deficit is expected to be financed by foreign loans and the remainder by the proceeds of asset sales by IBRA and the privatization of state companies. On February 2, Indonesia was pledged to receive new loans of $ 4.73 billion from the Consultative Group on Indonesia (CGI).

A budget is pledged to progressively lift subsidies, lower the country's unwieldy foreign debt and finance much of the hefty burden of recapitalizing bank with government asset sales. The budget for the nine months ending December 31, 2000 is concentrating on boosting domestic revenue from tax collection and asset sales in ways to reduce Indonesia's dependence on foreign loans. The projection on expenditures assumes a decline in subsidies, further restoration of public sector wages, and an increase in targeted social expenditure. In each of these areas, the FY 2000 budget takes an important step, as part of a multiyear effort, toward correcting distortions (for fuel and power), narrowing the wage differential with the private sector (especially for the upper echelons), and strengthening the size and governance of social sector expenditure. Risks to social stability from the tariff increases are to be minimized by protecting low-income households from their impact.

Implementing decentralization with fiscal neutrality will be a major challenge. FY2000 will be devoted to preparing for full implementation of this initiative during 2001. The authorities have, thus far, been able to resist pressure to advance decentralization into FY 2000, recognizing the considerable lead time needed to ensure a smooth and successful process of fiscal decentralization. Nevertheless, pressures to alter the planned sequencing and speed of decentralization are likely to persist, and constitute one of the major risks to the budgetary framework in FY 2000.

Banking and Corporate Sector Reform

The authorities recognized that the credibility of the overall program relies on the accelerating bank and corporate restructuring. Therefore, the banking and corporate sector reform needs to be carried forward in a much more integrated way than they have been in the past. Bank reform agenda aims at restoring a functional banking system with the strategic objectives: the completion of the recapitalization of all banks, the assurance that bank restructured at minimum public costs, the enhancement of supervision and improvement in governance in the banking sector, and the deepening of bond and equity markets.

In tandem with bank restructuring efforts, the authorities recognize that corporate restructuring needs to move ahead with much greater momentum in order to restart credit flows that are needed to sustain the recovery. To this end, the government intends to provide new political leadership and direction to the corporate restructuring strategy, improve the implementation of the bankruptcy law, enhance the governance framework in judiciary, instruct IBRA to intensify implementation of its sequenced strategy toward its corporate debtors, and strengthening procedures for non-IBRA-led restructuring.

Other Structural Reforms

The authorities recognized that insufficient observance to institution building over a long period led to a steady erosion in the governance framework for economic and social activities, contributing to the depth of Indonesia’s financial crisis, and burdening the recovery process. In order to command the trust of the people and allow the smooth implementation of the policy agenda, the Indonesian Government has committed to rebuild economic institutions by setting priorities on the public sector (fiscal management and civil service reform), financial sector (IBRA, the state-owned banks, and the regulatory and supervisory institutions), the judiciary, and the institutions responsible for corporate governance. A new national corporate governance strategy, developed in close coordination with representatives of the financial and business community, is finally nearing its completion.

Near-Term Outlook

Assuming the socio-political condition within the country improves and the economic players' confidence increases, as well as supported by stable rupiah, the authorities view that the economic recovery process in 2000 will be accelerated. Considering the above trends, based on the conditions of Fundamental economy and factors directly affected by the monetary policy, Bank Indonesia targets the core inflation rate in the year 2000 to be around 3 and 5 percent. The target does not include another estimated 2 percent inflation rate that could arise from planned fuel and power tariff increases and public sector wage adjustments. In order to achieve the targeted inflation rate, the authorities will carefully manage base money growth that corresponds to the real economic need. To this end, the authorities determine that base money growth to the end of 2000 will be 8.3 percent. The determination of inflation rate and monetary target also consider the prospect of economic growth and balance of payments. The authorities predict that the nascent economic growth will reinforce to the 3-4 percent range during FY 2000, rising from about 1.8 percent in FY 1999/2000 and the current account will achieve a surplus of 2.1 percent of GDP. The capital account should benefit from private inflows associated with improved confidence and greater momentum in corporate and bank restructuring.

Mr. Shaalan and Mrs. Farid submitted the following statement:

The momentous, though lengthy, transition to democracy as well as other difficult political developments, unfortunately caused an interruption in the implementation of Indonesia's economic reform program under the EFF. Nevertheless, it is noteworthy that despite the difficulties, macroeconomic stability has been broadly preserved and indicators show that a moderate resumption of growth is underway. Inflation remains low, interest rates have dropped to pre-crisis levels, the exchange rate has stabilized, and a comfortable cushion of foreign exchange reserves has been built up. Even the troubled banking sector has begun to stabilize even though progress in bank recapitalization and restructuring was more limited than originally envisaged.

The challenges facing the new government in pursuing the unfinished reform agenda remain daunting, however. Meeting these challenges will require not only an unwavering commitment to the implementation of the bold and comprehensive reform agenda adopted but, also, deft political skills to successfully guide important reform proposals to fruition in the new democratic environment. We therefore support the reformulation of the unfinished reform program as a new EFF that is fully owned by the new government. We are hopeful that this will result in a reinvigoration of the reform process and help garner broad public support for the difficult decisions that lie ahead. It is well to stress here that the task confronting the authorities is by no means an easy one, particularly since it is likely that many of the measures envisaged, particularly in the banking and corporate sectors and those entailing subsidy reductions, will elicit strong resistance from some circles. Tensions between regions and the central government are also likely to render the smooth implementation of the planned fiscal decentralization a challenging task. Throughout the reform process, a careful balance will need to be maintained between the dictates of preserving political stability and the need to press ahead with structural reforms to place the economy on the path of sustainable growth.

While we support the authorities' strategic medium-term objectives of an early elimination of dependence on exceptional financing and of improving the debt dynamics, the priority over the short term should be to firmly support the incipient and still fragile economic recovery. In our view, whichever of the methodologies in Box 4 is used to assess the fiscal stance, fiscal policy in FY 1999/00 and 2000 does not appear to be sufficiently supportive of the growth projections. First, it appears that the effect of the expenditure shortfalls in the first half of FY 1999/00 is unlikely to be fully compensated for during the second half of the year. The fiscal stimulus is expected to be close to zero, according to standard WEO methodology. Second, most methodologies also point to a withdrawal of stimulus in FY 2000. Our concern is heightened by the fact that since the start of the program overall deficits appear to have consistently fallen below program targets, keeping the actual fiscal stimulus lower than planned. The shortfalls also seem to be consistently in development and social expenditures, which point, at a minimum, to the need to assure reaching the targeted levels of these expenditures to secure both the sustainability of the recovery as well as the maintenance of broad public support for the reform process.

Turning to the FY 2000 budget, we strongly support the planned wide-ranging tax reform program which is expected to improve the efficiency and equity of the tax system and to lay the ground for broadening the revenue base. We particularly support the emphasis being placed on scaling back various tax incentives and exemptions as well as a tightening of tax administration. These are key tax reforms. We would also urge the authorities to stand firm against the proposal to continue the tax-free status of a number of islands or extend it to others, since the potential for leakage is great and could seriously undermine Indonesia's tax structure. On the expenditure side, we welcome the planned reduction in untargeted subsidies, namely through a start in addressing distortions in the pricing of fuel and power. As noted above, however, we attach high importance to offsetting the effect of these reforms on the most vulnerable groups through an increase in targeted social expenditure.

The prudent conduct of monetary and exchange rate policies can be credited with the successful reduction in inflation, the easing of interest rates to pre-crisis levels, and the significant appreciation of the rupiah since the onset of the crisis. Interest rates remain high in real terms, however, and should be guided further downward as confidence improves. Given the relatively conservative stance of fiscal policy dictated by Parliament's policy guidelines, it is all the more important that monetary policy be as supportive as possible of the nascent recovery. We, therefore, support the view that an appreciation of the rupiah to its long-run equilibrium value is not desirable in the short term. Further exchange rate appreciation at this stage should signal the need for a further reduction in interest rates.

The importance of accelerating the implementation of the unfinished bank and corporate restructuring agenda cannot be overemphasized. We therefore endorse the steps planned for implementation during this calendar year as outlined in the Staff report, and welcome the authorities' clear recognition, articulated by Mr. Harinowo in his most helpful statement, that this forms the core of the reform program. Nonetheless, we acknowledge that the agenda is formidable and its successful implementation will depend to large extent on a strengthening of public institutions as well as the building of political consensus to provide the backing necessary for difficult decisions that will inevitably be opposed by vested interests. The measures being taken to strengthen the Bank of Indonesia, IBRA and other oversight institutions are therefore extremely welcome. We also attach high importance to the steps aimed at ensuring the effective application of the bankruptcy law and the strengthening of the judiciary branch.

Finally, the remainder of the authorities' ambitious and extensive agenda of structural reforms covers the gamut of corporate governance, increased transparency of government activities, a new privatization program, reform of the electric power, oil and gas industries, and the reform of agriculture policies. While we cannot but endorse this far-reaching agenda, we would also caution against the real possibility of reform overload which could well have a negative impact on the reform process. A clear prioritization and sequencing of initiatives is needed. Such prioritization should take realistic account of the country's institutional capacity as well as political realities. Experience has shown that tempering boldness with realism and careful preparation is an invaluable ingredient of success.

We support Indonesia's request for an extended arrangement and warmly wish the authorities every success in the challenging period ahead.

Ms. Lissakers and Mr. Sobel submitted the following statement:

Indonesia made commendable progress toward recovery over the past year, facilitated by IFI support. But key reforms, especially financial and corporate restructuring, have only to a limited extend been implemented. Indonesia is now entering a decisive phase of transition. The new government's plate is full and economic reform is only part of the agenda. Yet, economic reforms must be urgently implemented to spur growth, preserve social stability, resist centrifugal forces, strengthen governance, create the rule of law, and avoid an explosion in debt dynamics. The framework for reform has been designed. It now needs to be forcefully implemented in a firm and determined way by an economic team working closely together with support from the top.

Bank Restructuring

Implementation of financial and corporate restructuring is the essential starting point for lifting the debt overhang and restoring economic health. Continuing delays and slow progress in restructuring the banking system are digging an ever-deeper fiscal hole for the government, undermining confidence in the financial system and preventing credit from flowing.

Estimated recapitalization costs continue to skyrocket for state banks and we must guard against the risk that recapitalization takes precedence over restructuring lest new rounds of capital be required that would further jeopardize the fiscal position. The rationalization of Bank Mandiri is making some headway; what has happened to the bank's profitability since it was recapitalized? Unfortunately, slow progress is being made in changing management at BNI, BRI, and BTN; could Bank staff update us and discuss whether these banks use international advisors as does Bank Mandiri. Also, we are not persuaded that the GoI is showing the requisite commitment to managing its stakes in state banks and continued political jockeying over who should exercise control is emblematic of this reality. The authorities must forcefully carry through with privatization of state banks.

The future health of the banking system will rest on sound private banks. Last year's private bank recapitalization was a key achievement, but more work remains to be done. What actions were taken against owners of Category A banks that failed to keep CARs above 4 percent by January 20? We welcome the efforts by the Attorney General to investigate those involved in the Bank Bali scandal. This process should be pursued forcefully and free of interference. The derailing of the Standard Chartered transaction sent a chilling signal to foreign investors, one only reinforced by PT Astra in blocking due diligence by a potential foreign investor. To begin addressing reputational issues and for IBRA to meet it asset recovery objectives, Bank

Bali should be privatized at once with foreign institutions participating in the bidding, and action should be taken to conclude the Astra deal.

The recent special audit of BI highlighted Fundamental management weaknesses. We welcome MAE's remedial plan. The audit's findings are another example of why the Fund must urgently pursue its work on safeguarding the use of IMF resources.

Corporate Restructuring

IBRA is key to bank and corporate restructuring. For more than one year we have repeated that IBRA should operate independently and free of political interference in pursuit of its mandate to recover assets in a transparent fashion. It is regrettable that we still need to make this same statement today. We hope that with the creation of the Financial Sector Policy Committee and IBRA now reporting to the President, these problems can be allayed.

IBRA must get on with the task of asset disposal, and debt reduction must be a part of the equation. There is no point in holding onto debts whose book value cannot be realized. We welcome the Coordinating Minister's indication that asset disposal, focused on the largest debtors, should be undertaken in a "quick but orderly" fashion. But this principle needs to be translated into reality. Our experience in the S&L crisis and plenty of examples around the world show that holding onto assets in anticipation of higher prices will lead to even lower prices tomorrow. IBRA must also start using its leverage to bring debtors to the table and force out of court settlements or insolvency, and it must do so in a transparent and professional manner without regard to the political connections of the debtor.

The key to making the out of court settlement process work for IBRA and the JITF is to implement bankruptcy laws in a predictable manner. The bankruptcy process should be facilitated by the ability of JITF and IBRA to refer cases to the Attorney General and the numerous anti-corruption initiatives aimed at ensuring an impartial and fair judicial process. The staff's efforts in this area are to be lauded, and the United States is studying ways of providing technical assistance to assist the Attorney General in implementing the Anti-Corruption Law.

A good framework for corporate restructuring is in place. The economic team must now use it by working together and ensuring that the JITF, IBRA, and the FSPC do their part.

Macroeconomic Issues

In a short period of time, Indonesia has gone from a tradition of avoiding domestic debt financing to a general government debt approaching 100 percent of GDP. The authorities will thus inevitably want to limit deficits and return to their tradition. But deficit reduction should not come at the expense of a social safety net for the truly needy. Instead, loan recovery and privatization must increasingly be relied upon to reduce the debt burden. We urge Indonesia to implement the reforms proposed by last year's FAD mission and to continue efforts to cut wasteful spending, including unnecessary subsidies. We share the staff's deep concern that fiscal decentralization be very cautiously managed, and we hope the authorities will be receptive to Fund TA in this area. On balance, we are struck by the enormous fiscal risks – if estimates of privatization proceeds, asset recovery, and tax revenues due to better administration prove overly optimistic, what will be done given the limited scope for spending reduction?

Bank Indonesia has done a good job in keeping monetary growth under firm control, thus helping support market confidence. Its independence must be preserved, and threats to BI's status will only jeopardize recovery. If confidence is restored and the rupiah appreciates, further interest rate reductions should be pursued. But Indonesia needs to build up reserves given the less than full coverage of short-term debt and that the ratio of months of imports to reserves is a less useful concept in a world of increasing capital flows.

Structural Issues

There are additional commitments in the program that merit special attention.

The measures to consolidate governmental agencies' bank accounts, take stock of and audit off-budget Funds, and require audits of private foundations are extremely critical steps that will contribute to increased fiscal transparency, especially of military operations. The authorities and the staff should ensure these provisions are forcefully implemented and rigorously monitored consistent with the LOI's timetable.

We welcome the long overdue completion of the first wave of audits of the four key state agencies and publication of the audits. Not surprisingly, they highlighted woeful performance, large inefficiencies, and enormous governance problems. The governance problems need to be pursued to the end. We thank the staff for Box 2. Could World Bank staff inform the Board of the strategy and timetable for the second round of special audits and if they support publication of the second round audits?

The authorities have again pledged to eliminate BULOG's import monopoly on rice in the context of the introduction of a 30 percent import duty. We had thought BULOG's monopoly was terminated a long time ago, and we hope the ad volorem duty can be eliminated as soon as possible. Also, the continued deforestation of Indonesia is an environmental disaster of epic proportion. The Reforestation Fund was long ago to be brought on budget and used only for supporting forests. It is thus worrying that there is a recommitment that the Reforestation Fund should be used for its intended purposes. There is a strong case for improved administration of stumpage fees. Could the Bank staff elaborate?

We welcome the new direction the authorities have embarked upon in seeking to address the IPP problems. But all eyes will now be focused on the ministerial team and on whether good faith efforts are undertaken to achieve negotiated solutions. Could the Bank staff tell us if the new ministerial oversight team has met and brought on board special advisors, and if any monthly meetings have been held between IFI staff and the oversight team?

In 1999, Indonesia became the first East Asian country to ratify all seven ILO core conventions. We welcome this, as well as other measures to grant Indonesian workers associational and representational rights. But recent reports indicate that progress has been slowed in at least some regions, especially in view of reports about workers being arrested and employers undertaking reprisals against workers for engaging in union activities. We urge Indonesia to adhere to its timetable to enact changes to its labor laws to give substance to its ratification of ILO conventions and to cease arrests and reprisals.

Monitoring

We support today's program. But this program faces enormous risks and we agree with the staff's decision to monitor it closely through bi-monthly reviews. This monitoring process will need to ensure that the program is well implemented so that high standards of performance are achieved. We will particularly be watching ahead of the next review to see that concrete steps are taken so that each and every part of the institutional framework for financial and corporate restructuring and improved governance is vigorously implemented step-by-step. A firm commitment by the authorities to the rule of law and strong vigilance against vested interests will be essential to demonstrate real and meaningful ownership of the program.

A Word of Appreciation

Finally, we thank the staff, not only the Indonesia team but also others from numerous departments, for their extraordinary effort in developing and monitoring this program. Indonesia's new EFF request is also Mr. Neiss' last appearance in the Board. We know that one of his first postings many years ago was as Resident Representative in Jakarta and that his almost monthly Indonesian treks since the beginning of the crisis have been a labor of love. His efforts to meet with all facets of Indonesian society to foster understanding of the Fund-supported program led to broad acceptance of the IMF and helped maintain some stability during the difficult transition period. This is a wonderful legacy. We thank Mr. Neiss for his many years of fine service to the Fund, the Asia Department and Indonesia.

Mr. Portugal and Mr. Mori submitted the following statement:

We welcome the resumption of the Fund's financial support to Indonesia's economic adjustment program under a new extended arrangement. This step will be very important to underpin international confidence in Indonesia's reforms and to catalyze the additional external financing. It will also contribute to the authorities' efforts to further the considerable improvements in macroeconomic performance already achieved in 1999 with a drastic reduction in inflation, the stabilization of the rupiah, a stronger foreign exchange reserve position, and indications of economic recovery. Progress has also been made in bank and corporate restructuring. We support the proposed decision.

At the current juncture, the main policy objective is to achieve a rapid and solid economic recovery. Mr. Harinowo indicates in his helpful statement that GDP growth for the whole of 1999 is estimated at 0.1 percent, which is still unsatisfactory in view of the sharp contraction in growth experienced by Indonesia. An acceleration of the growth rate is needed to reduce unemployment and to narrow the output gap, still at 8 percent. Fiscal and monetary policies are the main instruments to bolster economic recovery. But they need to be complemented by structural policies to ensure the appropriate functioning of the transmission mechanisms and better allocation of resources for poverty alleviation.

Fiscal policy continues to play a key role in sustaining domestic demand, particularly through spending in development and social areas. Still, as pointed out by Mr. Harinowo and the staff, the support for the recovery has to be balanced against the need to make progress toward the public debt objective. Public debt to GDP ratio has risen sharply from under 25 percent to over 100 percent of GDP in the process of restructuring the financial sector. The excessive expansion of private credit during the period before the crisis has been converted into public debt. Over the medium term, fiscal consolidation is required to reduce public debt to a more sustainable level.

On the structural aspects of public finance, we agree with the need for further actions to improve the quality of expenditure by improving the governance of spending programs, redirecting the allocation of funds toward poverty alleviation to promote interregional equity, and increasing efficiency in the provision of public goods. Moreover, fiscal transparency needs to be enhanced by identifying and auditing off-budget activities and bringing them under the consolidated budget. We also support the rationalization of policies governing tax holidays and free trade zones to keep the tax system from being used to promote or discourage specific sectors, industries, or regions, as these measures may give room for abuse and evasion.

We share the staff's concern regarding fiscal decentralization. The authorities should be prudent in its implementation given the potential problems raised in paragraphs 4 and 5 of Annex II, which were actually observed in other economies carrying out a similar process. The decentralization should be carefully sequenced, ideally phasing revenue transfers with simultaneous devolution of expenditures and associated functions, to avoid any net impact on the general government balance. The overall initiative needs to be carefully monitored to ensure fiscal neutrality.

On the external sector, the surpluses in the current account have been maintained by reduced imports as the result of the severe compression in domestic demand and external credit. Despite a significant depreciation of the rupiah, exports in terms of value are still below the levels achieved before the financial crisis--the decline in export prices has more than offset volume growth. As the economy gradually recovers, a rebound in imports is expected, but this seems less likely to be matched by export growth unless Indonesia's export markets improve significantly. In the event, for a smoother process of fiscal consolidation and economic recovery, exceptional financing provided by the international community will be required. As long as relations with creditors are normalized and the reform program evolves, a reflow of capital --including the flight capital-- tends to materialize. In the meantime, there will be a need for bilateral and multilateral creditors to contribute to fill the external financing gap. We are pleased to note that the residual gap has been covered, and the program for FY2000 is fully financed, as mentioned in the staff's very informative update.

Despite the fall in interest rates to the pre-crisis levels, the private sector has not benefited in full from this more favorable environment. Delays in recapitalization and increasing insolvency, together with continued uncertainty about credit-worthy borrowers, might have hampered the reestablishment of normal credit flows, and therefore the effectiveness of monetary policy to foster economic recovery. In the fiscal area, early reprivatization of banks and rapid asset recovery by IBRA are necessary to lessen the consolidation pace required to reduce public debt. Also, as noted by Mr. Harinowo, greater momentum in the restructuring process tends to affect favorably the expectations to restore private inflows, especially foreign direct investment, essential to strengthen the external accounts. As bank and corporate difficulties subside, output growth may be further supported by a recovery in private investment. Therefore, we share the view that corporate and bank restructuring continues to be an important component of the program for a steady economic recovery.

Mr. Morais made the following statement:

Let me thank the staff for these useful papers. The staff appraisal also provides candid advice on the way forward. Mr. Harinowo is reassuring in his statement on the unwavering commitment of the authorities to forge ahead with many difficult reforms. Recent developments in Indonesia are encouraging; political transition has been peaceful and successful, macroeconomic stability has been restored and there are indications of a modest recovery. The period ahead is challenging and requires delicate balancing of macroeconomic and social policies to strengthen the nascent economic recovery while consolidating social stability. We encourage the authorities to make use of their popular mandate and to translate their commitments into action.

The recovery is being driven by private consumption and restocking. We encourage the authorities to accelerate corporate and bank restructuring in order to stimulate private investment and promote exports and broaden the sources of recovery. However, such restructuring takes time and absorbs resources. Meanwhile, it would appear there is room for fiscal policy to continue playing an important role in nursing the recovery. Against this background, we are concerned that tightening fiscal policy at this stage may be premature and we hope there will be a recovery in expenditures, necessary to offset the fiscal stimulus that was kept low during the first half of 1999/2000.

Down the road, we agree that once corporate and bank restructuring gather momentum and export performance improves, fiscal consolidation should follow. In this regard, embarking on fiscal consolidation while stimulating decentralization may seem to be pursuing two conflicting goals. In addition, the huge debt burden, the cost of corporate and banking restructuring, the pressures for improving conditions of service in the public sector to deter corruption, and the resistance from vested interests against withdrawal of tax exemptions and reduction of subsidies make fiscal consolidation the most daunting challenge. In this regard proper sequencing of reforms is called for and we encourage the authorities to prioritize those aspects of decentralization that do not undermine the revenue base. Promoting public awareness of local studies that urge for the scaling down of tax incentives and abolition of tax holidays and the withdrawal of tax exemptions will promote some sense of domestic solutions to problems and enhance ownership thereby giving the authorities an upper hand in the face of vested interests, including frictions with the islands. Measures should also be taken to improve tax administration.

Regarding the high debt, the commitment made by cabinet and parliament to reduce reliance on exceptional financing is very encouraging. Nevertheless, there is need to be pragmatic and avoid pressures on the exchange rate. Moreover, liquid reserves remain low particularly in relation to short-term debt. Also, there is the danger that lack of external financing might force the authorities to take recourse to premature withdrawal of the fiscal stimulus.

Another bold step taken is to predicate the current budget on no domestic bank financing, which will help control base money, keep inflation low and slow down the growth of domestic debt. The authorities now need to pursue corporate and bank restructuring in a manner that minimizes the use of public Funds. In this connection, cracking down on corruption and vested interests, improving governance in the judiciary and accelerating privatization are not easy but very necessary reforms.

The immediate role of monetary policy in the recovery process seems unclear. The staff assess that normal credit flows have yet to resume given that delays in recapitalization and increased insolvency have given rise to lagged reduction in lending interest rates and therefore real interest rates remain very high. On their part, the authorities have halted further interest rate reductions until base money returns to the program path. We share Mr. Shalaan's opinion that monetary policy should be supportive of the recovery and that any further appreciation of the exchange rate should trigger reduction in interest rates. As the credibility of this program hinges, among others, on improving the health of the financial sector, giving priority to reforms in this sector will be important, and noting the now high government ownership of banks, we encourage the authorities to begin the process of divestiture and use the proceeds to retire debt. The steps being taken by the central bank to strengthen regulation, supervision and enforcement of international standards are welcome.

Finally, the program of the authorities deserves the support of the Fund. The downside risks, emanating mainly from the threat to the security situation and the difficulties in forging greater transparency are far outweighed by the authorities' great sense of ownership, their strong pledge to policy continuity that will be facilitated by the popular mandate accorded to the new government and the improvement in social conditions that will be derived from the recovery process. The staff's proposal for periodic assessments also provide an additional safeguard.

We support the proposed decision and wish the authorities well in their endeavors.

Mr. Mirakhor made the following statement:

We congratulate Indonesia for the completion of the Presidential elections and the smooth induction of a new government. As the lucid staff paper notes, these events, and the new government's pledge of policy continuity, have greatly diminished the political and economic risks to the program and have established a strong basis for continued implementation of the adjustment and reform agenda.

Macroeconomic performance during the eventful year of 1999 has been encouraging. The economy has stabilized amid signs of an incipient recovery, inflationary pressures have subsided and interest rates have declined dramatically. Market confidence has been bolstered by a significant turnaround of the external situation. More importantly, progress was made in the challenging area of bank and corporate restructuring. While the authorities deserve to be commended for these accomplishments, much remains to be done before the present recovery assumes a more durable character. We welcome the new government's bold and comprehensive reform program and support the request for a new extended arrangement.

The program is appropriately anchored on the twin pillars of macroeconomic stabilization and sweeping structural policy reforms. Its strategic objective is to eliminate Indonesia's dependence on exceptional financing and to seek improvement in debt dynamics—goals that we welcome and endorse. The staff note that on the macroeconomic level, the greatest challenge lies in the area of fiscal policy. We agree with this assessment since fiscal policy will have to deliver on a multiplicity of important objectives: striking the right balance between support for the recovery and beginning fiscal consolidation; strengthening poverty alleviation programs; ensuring good governance in the civil service; and achieving fiscal decentralization. These tasks will become all the more difficult in view of the high interest costs of financial restructuring. We welcome the planned improvement in the revenue-to-GDP ratio for FY2000 through the retrenchment of various tax incentives and holidays, the rationalization of VAT exemptions, and the proposed strengthening of tax administration. These are appropriate alternatives to potentially counterproductive increases in tax rates.

The expenditure side of the budget also includes a number of bold measures. In the area of subsidy reduction, it will be important to ensure that low-income households are adequately protected. On wage policy in the civil service, while we support the increase in compensation for a small group of senior officials as an essential adjunct of the government's anti-corruption drive, the risk of a ripple effect throughout the economy may deserve close attention.

The conduct of monetary and exchange rate policies has brought price stability and strengthened the domestic currency. These are impressive accomplishments indeed. Looking forward, we agree that as confidence improves and risk premia decline, there should be room for a further cautious lowering of interest rates. This would be especially helpful to the economic recovery in the context of a fiscal stance that had to be tightened. A sharper-than-desired appreciation of the exchange rate would also signal a need for monetary easing. While the staff feel that competitiveness is at present not at risk, the unevenness of Indonesia's export performance suggests that close attention to this issue—including the timely implementation of those structural reforms that have a direct impact on the productivity of the tradable sector—may be warranted.

We agree with the staff that the agenda for structural reform is so daunting as to strain the political will and administrative capacity of any government. The pressure on the new administration is "truly immense." As Mr. Harinowo recognizes in his statement, the credibility of the authorities' overall program—as well as the strength and durability of the economic recovery—hinges on accelerating bank and corporate restructuring. While there has been progress, the banking sector continues to pose risks to the program, requiring political consensus, the building of new institutional structures, and strengthened governance. If all elements in the bank restructuring agenda are implemented, there is a very real prospect of the emergence of a strong banking sector during the course of 2000. A concurrent challenge is imparting a new sense of urgency and momentum to corporate restructuring while ensuring that the bankruptcy law is applied in a fair and predictable manner. We support the initiatives planned in this area. We are pleased to note that the new national corporate governance strategy is nearing completion. We strongly support the government's initiatives in the area of transparency as they relate to quasi-fiscal activities and the auditing of key state enterprises and off-budget Funds.

We are reassured by Mr. Harinowo's statement that the Indonesian government will steadfastly and unfailingly pursue their reform program so as to strengthen the foundations for future sustainable growth. However, the authorities' own determined efforts will need the full support of the international community of which the proposed new extended arrangement is a crucial element. While political and economic risks remain, we agree with the staff that the new government is doing all that is feasible to address the risks and implement its program. Indonesia therefore deserves our full support.

Mr. Milleron made the following statement:

At the outset, I would like to commend the staff for the remarkable job they have done both in negotiating this extended arrangement and in drafting the presentation papers, which provide truly enlightening information on a number of intricate issues.

It is quite unchallengeable that Indonesia needs the Fund's financial support to put the economy back on a sustainable growth path. I also agree that this support should be provided without further delay, given the many tangible assurances already provided by the government that it is committed to implementing the right policies, in all areas. Clearly, the approval of this arrangement will be a key step in the restoration of financial stability in Indonesia.

Nevertheless, it must be underlined that this program is a high-risk one, for which an even more demanding structural conditionality and some amount of private sector involvement could be warranted.

On the main risks to the program

To begin with, recovery is underway, but it remains very fragile. Indeed, it is primarily driven by export growth, which makes it heavily dependent upon the economic performance of Indonesia's main trading partners. True enough, internal demand is expected to pick up in the course of this year, but unless the bank restructuring process accelerates significantly, private enterprises may soon face a credit crunch, which would stall recovery.

Moreover, monetary policy is set to be durably constrained by the cost of public debt service, which, on average, under the hypotheses of the program will amount to as much as 4 percent of GDP. In addition, 2/3 of the bonds floated to Fund the restructuring of the banking sector bear variable rates. On average, the real interest rate of public debt has been higher than the rate of growth of GDP for the last two fiscal years (1998/99 and 2000) and it is likely to be but a notch below for the remainder of the program period. Against this background, the authorities will find it extremely difficult to toughen monetary policy, should inflationary pressures arise. Unfortunately, such pressures are not unlikely, given the scheduled rise of a number of administered prices (electricity, basic commodities) and the salary increases announced for civil servants, which could spark contagion in other sectors. The easiest way out of this deadlock would be a significant appreciation of the rupiah, which, in the short run, will mostly depend on the political outlook.

Thirdly, the proposed trajectory for fiscal consolidation is built on hypotheses that could prove to be fragile. In particular, the small buildup of tax revenue envisaged (+ 0.9 percent over the program period) may not be sufficiently ambitious, in light of the uncertainties affecting the other revenue sources, in particular privatization receipts and IBRA asset disposal. On the expenditure side, as noted in the Staff report, the risks of slippage are also considerable, particularly on account of the political pressure to proceed with fiscal decentralization without an adequate framework and a comprehensive set of checks and balances. As well, in spite of the transparency initiatives announced in the letter of intent, private foundations performing quasi-fiscal duties, extra-budgeted accounts and nonfinancial state-owned enterprises are likely to remain a major source of uncertainty in the foreseeable future.

On the other hand, it is also quite clear that, at this stage, it would be premature to withdraw fiscal stimulus. These somewhat conflicting goals point to the need for the authorities to concentrate on making public spending more effective, which can be achieved by eliminating all the sources of leakage which have existed thus far and by better targeting expenditure.

On structural conditionality

As the staff made clear in their paper, the major challenges of the program are structural. The staff paper is quite comprehensive in coverage and explicit with respect to the measures which need to be implemented for the successful completion of the bank and corporate restructuring process.

However, in view of the many delays experienced thus far in the conduct of these processes as well as considering the magnitude of the tasks facing the authorities, we feel it is necessary to set clear benchmarks for the entire range of reforms to be undertaken, in order to make sure that momentum is not lost halfway through the process. In particular, it would be essential to convert into formal structural benchmarks the most important steps described as policy actions in Boxes 2 to 7 of the letter of intent, with a special emphasis on those related to corporate and bank restructuring, governance of key institutions and IBRA's asset recovery efforts. Short of doing this, the bi-monthly reviews suggested by the staff will do little to ensure that the program remains on track. In addition, it would be paradoxical to have tougher conditionality on the NDAs of the central bank, which are a traditional performance criterion in IMF programs, but not a critical one in this case, than on measures which are absolutely key to the sustainability of the program.

Also in connection with structural reforms, I would like to make two remarks related to the institutional setting. Firstly, since it appears that a significant proportion of banks are to remain within the public sector for quite some time, the way in which government is going to exercise its ownership is critical. In this regard, we see some uncertainty in the current situation, where the respective roles of the ministry of finance and of the ministry of state-owned enterprises lack a clear definition. Secondly, it must be underscored that the responsibilities imparted to the Attorney General are truly immense : to mention only the most prominent ones, he is expected to major role in the implementation of the judiciary reform, as well as in speeding up the corporate restructuring process, to make sure that an effective bankruptcy law system is put in place and to tackle the judiciary follow-up of the Bank Bali case. No matter how qualified and committed the Attorney General is, there is a high likelihood that he may become overburdened. Yet, these reforms are crucial. The Attorney General should be provided with all the support and budgetary means that are required in order to fulfill all his responsibilities.

On private sector involvement

Private capital flows are a major constraint for Indonesia's balance of payments. At the same time, the international community is expected to make a very significant effort to Fund the country's huge financing gap. Against this background, and bearing in mind the ongoing debate on the role of the private sector in the international financial system, I am a little surprised, to say the least, that the program hardly addresses the issue of private creditors.

The staff hardly mentions that the restructuring of corporate debt has not resulted, so far, in a net transfer in favor of Indonesia's enterprises, a state of fact which is quite objectionable. According to the Staff report, the only private creditors who might have to take their share of the burden are the banks holding government debt. But they are not the only ones. Other creditors to whom the Paris Club may wish to apply the principle of comparability of treatment include bondholders and all the creditors who took part in the exchange offer on interbank debt in 1998 (see below).

Furthermore, I would have appreciated some sensitivity analysis of the financing gap, in particular to variations in the price of oil, the weight of services excluding interest payments, the evolution of FDI and, more generally, capital outflows linked with private sector operations. In light of the very significant difference between the initial appraisal of the financing gap in August 1998 and the actual one, such a sensitivity analysis would have been warranted. Indeed, it should be recalled that in 1998, the very conservative assumptions made had resulted in massively overestimating the external financing need (by $4 billion just for the August 1998 – March 1999 period), thereby pumping up the effort expected from Paris Club creditors.

This time, Paris Club creditors agreed, at their last meeting, on the principle of negotiating a new rescheduling agreement regarding all debt repayments falling due between April 2000 and March 2002. But, according to the MOU of September 1998, this negotiation should start only after the expiration of the current rescheduling agreement (i.e., March 2000) and after Indonesia completes all bilateral negotiations related to it. Therefore, it should be possible to hold the new negotiation during the April session of the Paris Club.

This negotiation will tackle both the terms of repayments and the span of the debt taken into consideration. In particular, Paris Club creditors will have to decide whether or not to apply the comparability of treatment principle to bondholders, which had been left out in 1998 only for want of amortization falling due during the period covered by the agreement. They will have to make the same decision regarding the creditors who took part in the exchange offer on interbank debt in 1998. In this respect, the staff's contention that this operation was part of the public debt rescheduling effort (cf. par. 7 and footnote 3, p.11) can be quite misleading. Actually, those creditors were initially exposed to Indonesian banks, and subsequently obtained a guarantee from the State, which transformed these private liabilities into a potential expenditure for the State budget, but by no means changed its status into public debt. In this respect, it is unclear whether the repayments falling due on this debt in 2000 (close to $800 M) and 2001 ($1,3 billion) have been included in the analysis of the public debt service presented by staff in their paper. The staff's comments on this point would be welcome.

To conclude, I noted that the Staff paper strongly conveys the impression that collaboration on the field between IMF, World Bank and ADB Staff has been quite exemplary. This is good news, and it will certainly do a lot to help the Indonesian authorities meet the daunting challenges that await them. Indeed, these challenges are huge, but in many respects, not very different from the ones faced by other Asian crisis hit countries. Making bankruptcy laws work, recapitalizing banks, achieving progress with corporate restructuring, selling off the assets acquired by the public sector in the midst of the crisis are undertakings which are well underway in neighboring countries. Hopefully, the coordinated assistance of the IMF and of MDBs will help the authorities take advantage of the experience gathered abroad as well as within these institutions.

Mr. Taylor made the following statement:

During the first half of 1999 we observed a strengthening in Indonesia's macroeconomic performance. And conditions remained relatively stable for the remainder of the year, despite the suspension of formal program relations. We are therefore grateful for the staff's commitment to ongoing informal dialogue with the authorities, and the authorities' endeavors to keep things on track, during this period.

The challenge now is to build on these improvements with the objective of securing a stable, sustainably growing and efficient Indonesian economy. We therefore support the new extended arrangement for Indonesia. While the program is not without risks, we are reassured by the comprehensive set of quantitative performance criteria and indicative targets against which commitments under the program will be monitored. We consider it appropriate that the program include bi-monthly reviews during its first year. This is desirable for both ensuring Indonesia's success and, given the Fund's large exposure, for safeguarding the Fund's resources.

The program represents an ambitious and comprehensive blueprint for macroeconomic policy and structural reform over the medium-term, focusing strongly on the unfinished business of corporate and financial restructuring.

With the complexity of the program and the evolving political situation, it is understandable that not every policy action has been accomplished strictly on time. We would, however, like more details where it appears there may have been lack of political will, for example, difficulties with the appointments of ad hoc judges.

The process is certainly moving forward; for example, the recapitalization of Bank Mandiri and progress in resolution of the Bank Bali affair. Nevertheless, more needs to be achieved, particularly in the difficult areas of loan collection and asset recovery, and corporate restructuring.

We agree that the establishment by the Government of the Financial Sector Policy Committee should inject corporate and financial restructuring with a much needed high-level political impetus.

Looking forward, a major test of success in corporate and financial sector reform will be whether the Government achieves its own loan collection and asset recovery targets: an outcome which will be influenced by its preparedness to initiate bankruptcy procedures against non-cooperating debtors and the effectiveness of the judicial system in dealing with them.

Improvements in confidence are a critical assumption for many aspects of the program. Therefore, deadlines have an added imperative because they will weigh heavily on a turnaround in confidence and program outcomes. While not detracting from the importance of external financing and the catalytic role the Fund can play, we need to keep in mind that actions often speak louder than money alone. It is therefore important that IBRA performs well, better than it has been able to do to date. However, IBRA should be assessed against realistic timetables and objectives. On this score, we note that the staff considers IBRA's asset recovery targets for FY1999 and FY2000 realistic and achievable.

Further progress is also necessary with other structural reforms, including privatization and reform in the state enterprise sector, and the establishment of improved regulatory regimes and market-based pricing in the telecommunications, electricity, and oil/gas sectors. While the Government's 2000 Budget goes some way to addressing non-economic pricing practices in these areas, subsidies and price supports should be progressively phased out over the program period. In particular, we consider that there may have been some scope to move more quickly on the rice pricing front (without unnecessary detriment to the positions of rice producers). We would therefore encourage the authorities to reduce the rice tariff at the earliest feasible time, with an eye to achieving a better balance between poverty alleviation and the interests of producers.

We are supportive of the objective of fiscal decentralization outlined in the program. But, as the staff points out, the strategy entails risks. Its success requires that care be taken to ensure that an adequate framework is first in place to safeguard fiscal prudence. This will require proper institutions and reporting mechanisms conducive to improved standards of transparency, accountability, financial management and co-ordination across all levels of government. The designation of the Ministry of Finance as lead agency for implementation of this agenda, and the provision of a full time adviser, should help ensure that decentralization does not lead to a weakening of the Government's overall fiscal policy framework.

Indonesia has made good progress in controlling inflation. We note that the Bank of Indonesia injected substantial additional liquidity into the system late last year to deal with potential Y2K problems. While BI has been winding this back, we understand that, as of January 31, liquidity still stood at Rp87.7 trillion (i.e., around the target level for the end of the 2000). It will be important for the Fund to keep a keen eye on this to ensure that base money returns to the agreed program path, particularly in view of the sensitivity of the budget to interest rates and the importance of still faltering private investment to the recovery.

On wage policy, we acknowledge that there is the risk of possible flow-on effects of the proposed wage increase for senior officials. And, I agree that a more moderate increase would have been preferable, but for a somewhat different reason. The authorities argue that "any deferment would undermine" their anti-corruption strategy. In our view, they are perhaps putting too much weight on the role of large wage increases at this stage of the anti-corruption strategy. Such a strategy should ideally have a broader base—including guidelines and monitoring for accountability and responsibility—and be carefully sequenced. Thus, before the question of further wages increases arises, it would seem desirable to first examine comprehensively the structure of the civil service and ensure that the right people are being rewarded in the right way.

Mr. Schlitzer made the following statement:

We support Indonesia's request for an extended arrangement and have no problems with the proposed exceptional access level. In addition to providing substantial financial support on its own, the Fund's program can exert a catalytic force that can be especially helpful at this delicate juncture. Moreover, the Indonesian authorities have demonstrated their commitment by completing an extensive list of prior actions before coming to the Board (albeit a few could not be implemented). At the same time we cannot underestimate the high risk posed by Indonesia for the Fund. The recent banking scandals and the pervasiveness of the corruption problem require us to be particularly vigilant in monitoring program implementation.

The Indonesian authorities are embarking on a very ambitious and comprehensive reform effort, the success of which calls for a serious long-term commitment. In this regard, we continue to be grateful to the staff for the tremendous support they are providing to Indonesia. We fully share the thrust of their appraisal and also find the papers they have prepared for the Board to be of high quality. Perhaps a table listing all the required prior actions in the main report would have gone to the benefit of clarity.

Macroeconomic outlook

As noted by Mr. Harinowo in his helpful statement, macroeconomic stability has been broadly restored and a recovery is now apparent. Both remain very fragile, though. The economic recovery, in particular, is still consumption driven while investment appears restrained by an uncertain environment and a tight situation of the credit market. The growing current account surplus, notwithstanding a slightly improved export performance, is indicative of a still timid recovery.

Against this background, financial policies should remain strongly supportive of economic activity without jeopardizing the results achieved in terms of stability. Within these premises, the room to further reduce interest rates should be fully exploited. Fiscal policy should rely on targets and measures that can easily be calibrated to changing economic conditions. Hence, the envisaged withdrawal of fiscal stimulus should be seen as conditional upon the state of the recovery.

Fiscal issues

The fiscal stance is clearly key to the success of the program. A balance must evidently be struck between short-run stabilization and long-run sustainability. From standpoint, the ambitious medium-term objective of reducing the debt burden is commendable. A higher growth rate than anticipated should be used to seek an aggressive strategy of debt reduction.

It is unfortunate that social spending shortfalls occurred. Their effects are not limited to the macroeconomic domain, where the social spending underperformance has kept the fiscal stimulus unduly low. In the case of Indonesia ensuring that macroeconomic stabilization go hand in hand with social protection objectives may greatly reinforce the effectiveness of the program. In this regard we would like to know from the staff or the World Bank representative about the progress being made.

Understandably, fiscal decentralization must be addressed to meet the demand of the regions and provinces. But there is no need to say that the authorities should proceed very cautiously on this front to make sure that decentralization is not going to jeopardize the fiscal consolidation effort. They should therefore continue to resist pressures to advance the start of the process without the proper institutions being put in place.

On the proposed increase in wage compensation for a group of senior officials, we are somewhat skeptical that it can be used as the major anti-corruption device. The authorities should instead consider a wider anti-corruption strategy. Besides, they should closely monitor the potential demonstration effect that may result from the salary increase.

Bank and corporate restructuring

We note the authorities' commitment to move further in the process of improving the institutional capacity and governance of key financial sector institutions. The acceleration of the reform effort should help stabilize expectations. We welcome, in particular, the newly established Financial Sector Policy Committee, which will promote coordination among all the parties involved in bank and corporate restructuring. The FSPC will also enhance the role and the independence of the IBRA and JITF, in particular allowing more expeditious referrals to the Attorney General.

The governance framework for IBRA remains a very important piece of the overall design. We look forward to seeing the study undertaken with the assistance of the WB. We wonder, however, whether it could have been worthwhile to consider adopting a new governance framework for IBRA as a full performance criterion, and not just as a benchmark. Since the IBRA falls under the WB area of responsibilities, perhaps a performance criterion is envisaged in a WB program. Staff comments are welcome.

The issues of supervision remain critical and hard to overemphasize. As emphasized in the staff paper, handling the banking crises was impeded because for a long time no true picture of the banks' situation was available. On this front, we urge the authorities to take full advantage of the TA provided by the MAE and to promptly implement the advice offered.

We wish the authorities all the best in their future endeavors.

Mr. Collins and Mr. Taylor submitted the following statement:

We congratulate the Government of Indonesia (GoI) and the staff for reaching agreement on a new and strengthened program in a relatively short period. In particular, we welcome: the comprehensive nature of the program; he emphasis on goal-setting and the clear timetable for reform spelled out in the tables of the MEFP; and the central role for transparency and good governance, and, related to this, the priority placed on rooting out corruption.

Governance and corruption remain major concerns. It is common ground that tackling these systemic issues is essential to restoring international investor confidence. It is also crucial to maintaining the support of the newly-enfranchised Indonesian people. Effective and credible improvement in these areas will clearly be difficult, but must be vigorously pursued. Government leadership and consensus will be critical.

We are confident that the new Government is serious both in its commitment to the reform program, and in its intention to accelerate the implementation of core elements (e.g., bank restructuring and recapitalization, corporate debt work-out, and tax reform). But any lagging in reform in one area has the potential to negate reform efforts in the others and thus derail the whole program.

We welcome the clarification of the framework for restructuring the financial and corporate sector, and of the objectives amongst the main players. It is vital that the members of the new Financial Sector Policy Committee (FSPC) are objective and facilitate rather than obstruct the process.

Continued independence of IBRA needs to be guaranteed, and pressure intensified on the largest borrowers. Thus we welcome the moves to a more rules-based system for asset recovery (set out in paras 39-41 of the MEFP), but would appreciate more detail. We also welcome the fact that evidence of fraudulent activity and/or non-cooperation on behalf of debtors would rule out IBRA debt reduction.

Rapid disposal of assets is highly desirable both to ensure that they are put to better productive use as quickly as possible and to reduce the level of, and risks associated with, the huge debt burden. Opportunities for foreign investment in asset sales should be taken wherever possible. We have noted that the well-publicized difficulties regarding the Bank Bali sale have added to further fiscal costs. Moreover, it is clear that changes in management and ownership are likely to benefit all institutions to be sold by IBRA. It would be extremely undesirable if assets were repurchased at discounted prices by their previous owners (or proxies) from Funds spirited offshore during the crisis.

Paragraph 18 of the Staff report notes the need quote to build virtually from scratch an effective supervisory regime unquote. Is there any more information about the new financial supervision masterplan? What does the staff think can be done to limit risks in the banking system while inadequate supervisory capacity is strengthened? We obviously welcome intentions to bring supervision up to the Basel Committee's Core Principles, but hope that credibility will not be undermined in light of the past weakness of supervision and abuses of controls at Bank Indonesia (BI). We will obviously be looking for full implementation of follow-up measures to the recent audit (as set out in box 5 of the MEFP). There is also a clear need for rapid action to bring CARs to international standards in order to reduce the incentives for banks to conduct risky lending and stall on financial restructuring of bad loans.

Economic Assumptions and Conditionality

We note that a number of the economic assumptions in the program are on the cautious side. For example:

the rupiah remains well below the Fund's estimated equilibrium value (as set out in box 6 of the Staff report) and, whilst a return to equilibrium is undesirable in the short term, there does appear to be some upside potential, which in turn could have implications for the external financing requirement;

the oil price assumption for this year is just $18/barrel, well below the present level, so this is likely to provide an additional cushion on the fiscal and external accounts;

there is no forecast of a return of Singapore-based flight capital; and

there is a contingency of 35 trillion rupiah for Bank Indonesia recapitalization.

Whilst we understand the need for caution and recognize the uncertainty faced in dealing with Indonesia, it is clear that the authorities could have some margin in meeting the quantified targets of the program (for net domestic assets, central government balance, etc) as specified in Annex VI. Therefore, will the quantified targets be adjusted if the assumptions prove to have been too pessimistic?

Since the specified structural criteria are also fairly limited in their scope (i.e., simply publication of BI and state enterprise audits), we think that it is important to emphasize that at each review we will also be looking for clear results against all of the conditions specified in the MEFP boxes—success against these measures will determine the success of the program. (It would be unfortunate if Indonesia could meet its formal program targets despite lagging on its reforms because of overly cautious budget assumptions. Indeed, it would have been desirable to have had specific structural reform targets included in the formal performance review criteria. The previous agreement shows that it is still possible to meet macroeconomic targets while making little to no progress on structural reform.)

We support the overall macro policy prescription. As is noted, fiscal policy needs to strike a fine balance between supporting recovery and preserving fiscal sustainability.

Whilst the objective of fiscal decentralization is politically understandable, it clearly poses significant risks. For example, there is a clear danger that separatist pressure may accelerate the transfer of revenue to the regions ahead of expenditure obligations. Indeed, it is very difficult to believe that the provincial governments will be satisfied by a neutral transfer. So we very much support the caution over implementation, and encourage as much technical assistance as possible. The tax law revision will be important to clarify the system.

Moreover, the general objective of closing tax loopholes and exemptions, and addressing public sector leakage via audit follow-up measures will have to make a vital contribution to securing future sustainability. For example, oil and gas revenues could make a significant contribution over the coming period, as long as the abuses within Pertamina are addressed. Bringing foundations into the tax net is a positive move to address the problems of history. But, again, what matters most are deeds not words. Enforcing tax payment in practice, however, is often hard to achieve.

Finally on public spending matters, we welcome the strengthening of poverty-alleviation programs, including those targeted on ensuring access to health and education services; the GoI's intention to fine-tune its social protection programs and to improve the targeting arrangements and monitoring provisions to try to minimize abuse; and also the intention to involve communities more effectively in the management of the country's natural resource base.

The role of the Independent Commission for the Audit of State Officials will be key. The priority afforded to boosting the integrity in the judicial system is welcome, including the willingness to use prosecutions, given the vital role in implementation of the bankruptcy law. Increases in civil service salaries will not be sufficient to root out public sector corruption if the opportunities for such abuses persist, so greater transparency and the simplification of regulations and closing of loopholes is paramount.

The commitment to a further program of public sector audits is also important. But, again, the audits should be seen as a means to an end, and so the follow-up work should be closely monitored. We also welcome the renewed commitment to increasing competitive pressures in the economy, including via privatization and planned enactment of the new Competition Law by the Commission for Business Services, which ought to provide a further incentive to attracting new foreign investment.

The paper is generally clear and well-written, but there are areas where, nonetheless, greater clarity would have been helpful. For example, there is minimal attempt to explain Indonesia's further external financing requirement, despite everything being supposedly on course at the time of the 6th Review last August, and reserves remaining firm. Indeed, with the additional Fund money allocated for the reserves, to what extent is the projected level of purchases necessary—especially given the projected massive exposure of the Fund to Indonesia? A more detailed breakdown of the external payments schedule (including payments related to eurobond, interbank exchange offers, and INDRA scheme) would have been helpful. The presentation of figuring is also inconsistent and confusing, jumping around in its use of rupiah, U.S. dollars, SDRs and percentages of GDP. And, for such a delicately balanced program, it would have been helpful to have been presented with possible outcomes under more and less rosy assumptions.

Mr. Toyama made the following statement:

I welcome that, thanks to the authorities' speedy and appropriate policy implementation, Indonesia's macroeconomy has started to show signs of recovery. I also want to thank the staff for offering appropriate advice during the transition period in order to solidify consistent economic policy. Future tasks for the authorities will be to actively tackle fiscal consolidation (including domestic resource mobilization) and structural reform (banking sector reform, and corporate sector restructuring), to restore stable and sustainable growth. This EFF program seems to be well focused on the above-mentioned issues. It is true, however, that the program is not without risks. I must stress, though, that the authorities are in a critical stage in proceeding with structural reform in light of long-term economic recovery. With hopes for strong economic recovery through coherent and timely implementation of economic policy by the new economic team, I support the proposed decision. Now, I will comment on some issues.

On fiscal policy, the important question is how to proceed with the transition from fiscal stimulus to fiscal consolidation. In this regard, I concur with the staff that the

FY 2000 budget is well balanced. I welcome that the authorities are attempting to establish methods for domestic resource mobilization, resulting in increased finance of the fiscal deficit with domestic resources, and reduced dependence on overseas aid. To establish methods for this mobilization, it is paramount to raise tax revenues through tax reform and improved tax administration, and to increase non-tax revenues such as asset recovery by the IBRA. In addition, it is also critical to secure stable issuance of medium- and long-term domestic bonds in order to mobilize domestic saving in an effective and efficient manner. Considering that banks will be permitted to sell government bonds in the course of recapitalization programs in the near future, it becomes much more important to establish a bond market.

Fiscal decentralization is expected to begin in 2001. As preparation time is limited, this is a very challenging task. Fiscal decentralization means not only transferring the revenue base, but also transferring expenditure items. In deciding this division of labor, several considerations will be required. For example, the administrative capacity of the local government and resource needs in each region should be taken into consideration. Therefore, they should proceed carefully, paying due attention to the sequencing.

Concerning a wage increase, it is an absolute necessity in tackling the governance problem. In this regard, I highly appreciate that the authorities are committed to ambitious anti-corruption measures. Giving due attention to its effect on the fiscal balance, they should undertake the governance problem intensively.

Regarding banking sector reform, the IBRA should function as expected. Therefore, it is critical to secure independence from political interference. I must stress that the IBRA plays a huge role in promoting corporate debt restructuring, strengthening fiscal balance, and increasing FDI to Indonesia.

On corporate restructuring, it is paramount to strengthen the JITF and to improve the application of the New Bankruptcy Law under impartial judges. While the issue of Bankruptcy Law is discussed in FSF, I hope Indonesia can become a model case in this area.

As my authorities have indicated in the CGI, we strongly supported Indonesia's economic recovery through the New Miyazawa Initiative, and so now we continue our active support for economic reform in cooperation with the international community.

Mr. Wei made the following statement:

At the outset, I wound like to thank the staff for the well-written report and their informative briefings to the Board on Indonesia's situation and policy stance, which have enabled us to follow Indonesian economic development closely and in a timely manner. Since the Sixth Review under the current Extend Arrangement, substantial progress has been made on Indonesia's economy. Over the past few months we are pleased to see that the recovery has gained momentum: inflation has been kept low, the rupiah has appreciated in nominal terms compared with the crisis period, the foreign exchange position has been strengthened, and market sentiment has improved as evidenced by rising equity prices and the declining risk premia. As mentioned in Mr. Harinowo's very helpful statement, the smooth completion of the Presidential election and the appointment of the new government is providing a stable political environment for further economic development and reforms. For all this, the Indonesian authorities should be commended.

With broad agreement on the thrust of the staff, I would like to make just a few comments for emphasis.

As we learn from the staff, the proposed new three-year program provides considerable continuity with the macroeconomic strategy of the present program where substantial progress has been achieved(increasing the focus on banking and corporate restructuring, the rebuilding of economic institutions, and poverty alleviation, all of which are essential for long-term sustainable growth. The new government's firm commitment to maintain macroeconomic stability and carry out reforms while developing new mechanisms to protect low income households is gaining popular support for the new program. With these general remarks, let me turn to the specific policy issues.

On fiscal policy, the authorities' putting more emphasis on scaling back debt and reducing dependence on external financing in the process of choosing the fiscal deficit target for FY 2000 is fully understandable, given the importance of fiscal consolidation in meeting future expenditure demands resulting from structural reforms to be carried out in the coming period, including banking sector restructuring costs, public sector wage increases, and the government's efforts to reduce its potential influence on fiscal decentralization. However, we share the concerns expressed by Mr. Shaalan and others in their statements that some more fiscal support is probably necessary in order to sustain and accelerate the recovery which is very important for the authorities to solve the issues of poverty and unemployment. We welcome the authorities' decision to reduce the untargeted fuel and power subsidies during 2000, which, together with the wide-ranging tax reform program designed to improve the efficiency and equity of the tax system and lay the basis for rebuilding the revenue base, will promote fiscal consolidation from both sides. This Chair shares the staff's concern on the complexity caused by the fiscal decentralization initiative. Close monitoring and further review are necessary in this regard.

Second, on monetary policy, while we welcome the progress in interest rate movements ending the negative interest spread between lending and deposit rates, we share the staff's view that, with the high real interest rate level compared with other regional economies, there might still be room for downside interest rate adjustment to support further recovery with the favorable external environment, declining inflation, and appreciating currency on the domestic front. However, the stimulus of a lower interest rate to recovery should not be overestimated since normal credit flows have yet to be resumed along with progress in banking sector reform.

Third, the comprehensive and detailed package of banking sector restructuring measures given in the MEFP and Boxes 3-5 indicates the authorities' strong will to accelerate the delayed pace in this area and to restore confidence. In this respect, we are encouraged to learn from Mr. Harinowo's statement that the authorities will carry forward the banking and corporate sector reforms in a much more integrated way than before, with clearly designed strategic objectives and measures in these two closely linked areas. Given the difficulties of carrying out the reforms, we encourage the authorities to make great efforts toward the full implementation of the envisaged plan, which is also vital to mid-term recovery and growth.

With these remarks, we support the program and wish the authorities great success in implementing the program.

Mr. Kiekens made the following statement:

A huge amount of work still awaits the authorities. They must finish dealing with the consequences of the crisis, and they must preserve popular support for the far-reaching reforms already implemented and still to come. It is reassuring that a new, democratically elected government is taking over this task. But as the staff observes, the challenges for the relatively inexperienced new team will be immense. Its determination to push ahead with a wide range of reforms adds further to the Fund's and the World Bank's responsibilities for the program's success.

The program is well-crafted, realistic, and sufficiently ambitious. It may even be too ambitious in the structural area, given Indonesia's limited administrative capacity and the need to focus on the core issues, particularly the banking sector and the restructuring of the debt. But let me first turn to macroeconomic policy.

The Asian crisis has revived the discussion about the role of fiscal policy in turning recession into recovery. Sixty-four years ago today, Keynes published his famous General Theory. The strength of his insights is confirmed by the fact that today we are again discussing the validity of policy prescriptions which he pioneered so long ago. This also shows how closely the situation in some parts of the world has recently resembled the Depression Era of the 1930s during which he formulated his policy prescriptions. We are fortunate that nowadays his advice about expanding public demand in times of insufficient private demand and widespread underutilization of resources is seldom relevant.

The staff notes that in Indonesia fiscal stimulus has accomplished less than intended. The experience of other Asian countries has been similar. It shows that there are limits to what fiscal expansion can accomplish without wasting money. In Indonesia, even though fiscal deficits have been lower than targeted, public debt has risen to 96 percent of GDP, 12 percent higher than projected at the sixth review last August. With public debt higher than programmed, the high interest costs will make it harder for the authorities to continue avoiding monetary financing. I therefore think it appropriate that the authorities are already beginning a gradual fiscal consolidation. Support for the recovery must now come from structural reforms, debt restructuring, bank consolidation, and as easy a monetary policy as is consistent with price stability.

Given the need for gradual fiscal consolidation, I am worried about some aspects of the fiscal reform. I share the staff's uneasiness about the planned increase in civil service salaries. I understand that wage increases can reduce the temptations of corruption for civil servants. But increasing civil service salaries may prompt other wage earners to demand similar increases. In that case, the differences between public and private sector wages will not be reduced and the authorities will be chasing a moving target. Zero tolerance of corruption in public officials, particularly the highest, should be the first line of defense against such behavior.

There are other fiscal policy risks as well. Serious problems lurk in the centrifugal tendencies that threaten Indonesia's territorial integrity. The government must pursue fiscal decentralization with great caution and strict adherence to the principle that decentralization of revenue allocation has to go hand in hand with decentralization of spending. The staff is rightly concerned about the authorities' intention of extending the tax-free status of several islands, given the difficulties of preventing large leakages. By publicly opposing these plans, the Fund might be able to help the authorities resist the pressure to expand tax-free status. I welcome the planned reduction of tax exemptions and tightening of tax administration. Both are better ways of increasing revenues than raising tax rates. However, this may not be enough, particularly if the recent increase in oil tax revenues turns out to be only temporary.

I agree with the monetary framework. The recently earned credibility of monetary policy should be further strengthened. Stronger credibility and falling interest rates will promote economic recovery and fiscal consolidation. Maybe the monetary program for 2000 is actually too restrictive. It is now expected that in December 2000, base money will be 8.5 percent higher than the program level for last December. This implies that base money growth will probably lag somewhat behind nominal GDP growth.

The staff sees room for interest rates to fall to a level well within single-digits. However, interest rate increases in industrial countries are likely to prevent Indonesian interest rates from falling much below 10 percent without creating pressure on the currency.

I agree that the appreciation of the rupiah should proceed gradually. There is still a good deal of slack in the economy. Because the fiscal stimulus must be withdrawn, it is desirable for the rupiah to remain below its estimated long-term equilibrium position for some time. If the rupiah appreciates too quickly, careful analysis may show that some further monetary easing is called for.

In sum, Indonesia's macroeconomic policies seems well balanced and on track.

There is much less reason for satisfaction with progress on structural reforms, particularly bank and debt restructuring. The high levels of unresolved debt and nonperforming bank loans remain a principal obstacle to strong economic recovery. The mechanisms for dealing with debt overhang should be strengthened soon. I am glad that the program is ambitious in this respect. The priority is a resolute and rapid recapitalization and reprivatization of banks. This will unlock new bank credit, enabling investments and exports to pick up and to supplement the stabilizing role of consumption. Indeed, it is remarkable how little consumption declined during the crisis. However, consumption alone can no longer carry the burden of sustaining the recovery. Indonesia cannot continue to draw down its savings.

A second priority is progress with asset recovery. This is crucial for financial stability. Public sector debt has exploded as a result of providing liquidity support and recapitalizing the bankrupt banking sector. The public debt must be quickly reduced by recovering as many assets as possible in the shortest possible time. If not, public investment and other priority expenditures will have to be curtailed, to the detriment of growth.

I join other speakers in encouraging the Indonesian authorities to make progress in increasing fiscal transparency, complying with core ILO labor standards, and to use the reforestation Fund efficiently for its intended purposes. Mr. Milleron is right when he suggests that monitoring of this program would improved by greater reliance on structural benchmarks and performance criteria.

The staff candidly admits the high credit risk for the Fund on Indonesia. These stem from the large amounts involved, the debt dynamics that await if program implementation should falter, and the political risks stemming from the present centrifugal tendencies in Indonesia. However, the Fund should neither attempt to avoid this credit risk, nor deny it existence when assessing the required level of precautionary reserves.

The Fund's present relations with Indonesia are a good illustration of the many reasons you have given, in your recent testimony before the Meltzer Committee, why the Fund is needed: foremost, to help countries implement good policies for their own benefit and that of their trading a financial partners everywhere. Although in Indonesia nowadays the Fund financial involvement is significant, this is far from the only way that the Fund promotes good policies. From last August until April this year, 48 IMF missions to Indonesia have taken place or will take place. Most of them involved technical assistance. The Fund maintains no less than three resident representative and three long-term experts in Indonesia. I expect that the Indonesian authorities are making good use of all this help. I would like to see reports on the effectiveness of our TA on the occasion of Indonesia's next Article IV consultation.

Indonesia is requesting credit totaling about $5 billion. This is acceptable, since it represents about 10 percent of Indonesia's gross balance-of-payments needs during the program period. This sharing between the Fund and other creditors of the burden of financial support for Indonesia is in line with standard practice. However, I noted the comments of Mr. Milleron about burden sharing between Paris Club creditors and private bond holders. As a general rule, it is preferable that the staff routinely calculates and includes in its reports to the Board every country's gross balance-of-payments needs, as justification for the proposed access.

There is no doubt that the structural component of this program is important, as is the case with almost all IMF programs nowadays. Moreover, Indonesia's balance of payments is likely to remain problematic for an extended period. I can agree to give Indonesia financial support under an EFF. However, I regret that the staff did not provide any specific justification for EFF access, nor any projections of the balance of payments situation beyond the standard three years. I think any request for an EFF should be explicitly justified in the Staff report.

For countries that continue to face balance of payments problems beyond the normal repurchase period for stand-by arrangements, it is preferable that the Fund should provide the necessary extended assistance through a follow-up program, as was done for Mexico, rather than through extended repurchase periods granted under EFF arrangements. Admittedly, this issue will have to be discussed more thoroughly when we review the Fund's lending instruments.

Finally, Mr. Chairman, I am very pleased to associate myself with Ms. Lissakers' kind words of praise for Mr. Neiss.

Mr. Hendrick made the following statement:

I would also like to commend the Indonesian authorities on their success, despite the difficulties with the political transition, in implementing a new arrangement and structural reforms.

The Bank of Indonesia has played an important role in reducing inflation and interest rates and maintaining a stable exchange rate. Additionally, the encouraging signs of economic recovery, described in Mr. Harinowo's statement, have set the stage for a swift recovery for 2000 and beyond.

Nevertheless, as the staff and the authorities recognize, the challenges to bring about expected changes will require strong commitment to policy implementation. We are confident that the new government will do its best to deliver. Accordingly, we support their request for a new extended arrangement.

Thanking the staff for a clear and concise paper for today's discussion, Directors in their statements agree on the policy actions. I join the consensus and would like to make some comments for emphasis:

First, on the request for a new extended arrangement. I am not clear why there is a need for a new EFF. The target for the third year of the current EFF could have been reviewed in light of the recent values and access to financing could have been granted under the current arrangement. A new arrangement could have been considered by the Board after the current one expires. The staff comments are welcome.

Second, there is no doubt that an efficient solution to the banking sector problem is necessary. Looking at the paper prepared by MAE on progress in bank restructuring, it is clear that the increase in the state participation of the banking sector to 70 percent calls for further efforts in the privatization program. This is critical, not only because of the increased amount of public Funds involved, more than 50 percent of GDP, but also because asset liquidation is important for the financing of the fiscal deficit and, therefore, for the reduction of the already high level of public debt.

Restructuring of the corporate sector is another important issue. Access to domestic and foreign credit also needs to be restored to allow for new investments. The consumption recovery will have to be complimented with new investment. Currently, "without strong investment and private initiative the Indonesian economy will not be able to get a grip on itself". For that purpose progress in restructuring of the banking sector will be critical to gaining investor confidence.

As, there is a consensus that this is a high-risk program, like Mr. Milleron, I believe that it is important to have some sensitivity analysis of critical barriers, such as the financing gap, particularly in a program with high access to Fund resources.

I welcome the authorities' success in attracting bilateral support but would like to know what other sources of financing might be available if the private sector, who were part of the original debt in 1998, refuses to reschedule the payments in 2000 and 2001.

I welcome the Bank of Indonesia slowing the reduction in interest rates. Although I agree that current monetary conditions call for caution in this regard. As Mr. Harinowo points out, the interest rates have already fallen substantially to the pre-crisis level. Therefore, there should not be a pressing need to go further in that direction.

On government corruption. I commend the authorities for their commitment to the rebuilding of economic institutions as reflected in the national corporate governance strategy, which is in the final stage of preparation. In this regard I share Mr. Schlitzer's skepticism whether increasing wage compensation for a group of senior officials may have a sizable impact on the anti-corruption efforts. I am not opposed to such an increase, but the anti-corruption efforts have to be employed across all levels of public services. Looking at box five of the main Staff report, I do not see a crucial difference between the majority of the civil service and between public and private wages, as opposed to some industrialized countries; 73 percent relative public to private wage is not a huge difference. The staff comments are welcome.

On statistics, I wonder if the staff can use calendar years as an outlook in the tables. Also, given the range of the inflation targets in Table 1 for the period 2000-2002, I would like to know if that problem is consistent with the lowering of the range.

Finally, I would like to associate myself with the gratitude to Mr. Neiss as expressed by Ms. Lissakers.

The Deputy Director of the Asia and Pacific Department made the following statement:

The basic motivation for a new three-year arrangement on the part of the authorities and the staff was to cover ownership. This is a new government and it is important for both sides that the authorities own this ambitious program.

As can be seen from the supplement, the staff focus on a large number of initial actions to ensure that the program is implemented across a broad front. The program contains about six structural benchmarks for the next five months. While for now only one structural performance criteria exists, as the program develops and in subsequent reviews, the staff would add more. In particular, there is a need to move from a widely based program, necessary to start it and to give full ownership, to a clear prioritization refraining from policy overload and focusing on the essentials. This process of distilling will be the essence of the early reviews. The staff have a range of dates in seven boxes in the LOI, of which not all will be met, but it is crucial for the government to move across a wide front.

On fiscal decentralization, currently the process was undergoing preparatory steps. The staff would appoint, in agreement with the Minister of Finance, an advisor to lead the exercise on the fiscal implications within the government. The Fiscal Affairs Department in conjunction with the authorities will hold a seminar, as dissemination of information and education are an important part of this process. The first priority is to ensure that the facts and the risks are well known.

On the monetary program, the staff had carried out a sensitivity analysis, but did not present it in this staff paper. However, it would be included in the next report. The staff had found that the usual parameters' effects, such as the oil industry or interest rates, on Indonesia's financial and balance of payments situation, were insignificant compared to the large uncertainty stemming from private capital. However, it was not easy to carry out a sensitivity analysis on private capital. The staff's scenario assumed a progressive return of flight capital, but uncertainties which were difficult to capture existed for Indonesia. The staff would, however, concentrate more on debt operations next time. Generally, the staff expect that the targets of the program will be exceeded, and that private capital will return sooner. However, if upside risks arise, and if there is no doubt that the current program will be too tight, the staff will address the issues again. That was convenient in Indonesia's case because of the frequent reviews.

Concerning the fiscal accounts, if the staff estimates in asset recovery prove to be overly optimistic, the fiscal program would be adjusted in light of uncertainties, but it is difficult to anticipate every uncertainty. However, the program will depend on the state of growth and the recovery. If higher revenues occur because growth is higher than expected, then that opportunity should be taken to scale back the public debt. If growth is moving less well than expected, then the automatic stabilizers should set in, and a higher deficit should be incurred. There was still some room in reaching the 5 percent fiscal deficit envisaged in the current program. In any case, the staff and the authorities should guard against any temptation to cut development and social spending. Within these parameters the staff have to establish how the fiscal program needs to be adjusted.

On the Fund's role in meeting the financing requirement and uncertainties that may arise in the financing gap, it is evident that Indonesia needs a recovery and a budget stimulus. But because inflation needs to be kept fully under control, a fiscal deficit of about 5 percent should be incurred and domestic financing avoided. This means that the resources available from the CGI, bilaterally and from multilateral institutions should not be used to build up reserves, but as a priority should be used to finance the budget. Additionally, Indonesia is slower than other countries in the region in strengthening its external situation, and therefore Fund resources will boost reserves. Nonetheless, at the end of the three year program, short-term debt will barely be covered, which has already occurred in the other countries. The level of access is designed to raise gross liquid reserves to slightly above 100 percent of short-term debt. Liabilities arising from the interbank exchange offers constitute a private transaction and are therefore not included in the public debt.

In general political will is crucial for the success of the program. A risk exists in that regard as it is unclear whether the government will move decisively against debtors.

The staff representative from the Monetary and Exchange Affairs Department made the following statement:

Bank Indonesia is aware of its need to rebuild its supervisory capacity and traditional supervisory function to maintain a sound banking system. Since last summer the authorities have been working with MAE on identifying key priorities, such as onsite and offsite special surveillance techniques.

Joint plans for implementing a supervision “Master Plan” are close to finalization between MAE and Bank Indonesia’s management. Part of the program will be supported by extensive technical assistance, and about five full-time experts will be supplied by MAE and other institutions to Bank Indonesia within the next few months. They will be supported by short-term experts to address specific issues.

In the meantime, to safeguard the banking system until the supervisory capacity has been fully established again, most banks are operating under a business plan which was designed with the assistance of external advisors. These plans are being monitored on a quarterly basis by Bank Indonesia, with a key objective being that all banks reach an 8 percent capital adequacy ratio by end-2001. MAE is helping Bank Indonesia to monitor this exercise. Surveillance will concentrate on the most important banks.

IBRA’s strategy for loan collection and asset recovery is largely rules based. Borrowers are being addressed from the largest to the smallest through a month-by-month schedule. Uniform criteria exist for treating the four different categories of debtors. But concerning the asset recoveries, limits exist regarding the speed of the asset sale negotiations.

Bank Mandiri was only recapitalized in December, but was making losses during the period prior to that at a lower rate than the interest receipts which it will have earned since the government’s issuance of the bonds. On that basis, it could be expected that Bank Mandiri has been profitable since recapitalization, but no firm data exist as yet.

The Deputy Director from the Policy Development and Review Department said that while the proposed access was high, it was not higher than had been envisioned in the previous program. The new program would ensure that Fund exposure was lower than had been the case in recent years, also when compared to Mexico or Korea during the early stage of the Asian crisis.

As concerned the issue of burden sharing, the Fund's share of the total amount of transfers since the beginning of the crisis was high, but would decline over the period of the new EFF arrangement.

Mr. Kiekens while agreeing with the proposed access level, noted that he had generally made the observation that the staff papers justify that level only in terms of quota. He was of the view that more relative indicators to justify the access would be more useful, such as an estimate of the gross balance of payment needs for Indonesia. He suggested that staff papers should include a calculation of the balance of payments needs and that the proposed access should constitute a percentage (5-10 percent) of those needs. Also, more explicit communication to the Board on the reasons for a proposed access level, taking account of all relevant parameters and not only quotas, would be helpful.

The Acting Chairman said that was a good suggestion.

Mr. Sobel said that in the future the focus should especially be on the audits, and agreed with Mr. Kiekens that the determination of the access level based on the gross financing need was a useful idea.

Mr. Donecker, however, warned that the access level should not only depend on the balance of payment needs. Policies on Fund access were related to quota foremost and also took account of the strength of the authorities' adjustment efforts.

The staff representative from the World Bank made the following statement:

> On the strategy and timetable for the special audits, my understanding is that as spelled out in the letter of intent, those will take place by the end of June. There was a commitment by the authorities, that the Bank supports, to ensure that these findings will be made public. The full modalities about which enterprise is going to be included in the second round of audits and the precise dates are still being discussed.
>
> Considerable commitment also exists to make progress, in consultation with major stakeholders, for improving the implementation of the various forestry and natural resource tax arrangements. The modalities of how that is going to be organized will depend on the outcome of the consultations. The authorities have asked the Bank to assist them with setting up further stakeholder negotiations, and the Bank will arrange a first meeting before the end of February. As part of that process, an inter-ministerial group is to be set

up, but has not met as yet. However, the Bank staff have been meeting with individual ministries that will participate in that team.

On social protection, this area was emphasized by all member during the consultative group meetings, and progress is being made. The Bank has disbursed the first tranche of the social protection operation in the amount of $300 million, which includes some co-financing. Principal improvements have been made in the area of consolidating various programs, improving the targeting, establishing the complaints resolution mechanisms. In terms of the implementation of the programs and making Funds available at the beneficiary levels, the difficulties experienced early last year have now been overcome. A number of improvements have been made to the administrative mechanisms by which some of these programs are being implemented. For example, some changes were being made in the way in which the scholarship programs can be collected at lower levels, operating through the post office, so that school representatives can collect the scholarships for all of the students at the same time, rather than dealing with them individually.

While we noted a sharp rise in the overall level of poverty associated with the crisis, the most recent information is that, while still high, the level of poverty has stabilized and has started to decline. As the recovery intensifies, we anticipate that that will have an impact on reducing some of the social costs.

In terms of the social protection objectives, various discussions on how to protect disadvantaged groups from the elimination of some of the subsidies have taken place. Broad consensus has been achieved that use of the rice distribution scheme is an efficient mechanism — with the exception of smaller subsidies, where some alternative mechanisms might be required.

Mr. Alosaimi made the following statement:

It is indeed encouraging that Indonesia’s adjustment and reform effort is beginning to pay off. Last year, the economy showed signs of a budding recovery in an improved macroeconomic context of decelerating inflation and higher external reserves. However, the recovery is still fragile and will require continued policy support. The new Indonesian authorities’ adoption at this juncture of the proposed bold and comprehensive program is a reflection of policy continuity that deserves international support.

I thank the staff for providing a very informative and well-written report for today’s discussion. I have concerns, however, whether the program, while clearly demanding, is also realistic. The report makes repeated references to limitations of the authorities’ implementation capacity. At the same time, the report stresses that the proposed program is ambitious enough “to strain the political will and administrative capacity of any government.”

Indeed, paragraph 79 explains that there are sizable risks to the program. This raises the question whether the program goals are unduly ambitious.

Turning to the policy agenda, the authorities are right to aim at early progress in fiscal consolidation as well as improvement of the debt profile, including reduction of dependence on exceptional external financing. However, like Mr. Shaalan and Ms. Farid, I see fiscal support for the still fragile recovery as a higher immediate priority. Regarding the current budget, I welcome the proposed tax reforms and the envisaged reduction of untargeted budgetary subsidies. On wages, I share the staff concerns over possible adverse repercussions of ad hoc increases in the salaries of senior personnel. Wage policy should indeed be considered as part of a broader strategy for improvements in civil service efficiency.

Resumption of the downtrend in interest rates is evidence that the authorities' combination of monetary prudence and exchange rate flexibility is working well and should be continued. Given continued absence of inflation, there may be scope to lower interest rates further. The authorities should therefore monitor the situation closely for provision of as much monetary support for the recovery as is feasible.

The difficulties that have arisen over major banks such as Bank Bali are a standing reminder of the costs from further delays in banking reform. Increased focus on bank restructuring, recovery of outstanding loans, privatization, and supervisory reform are critical for an effective functioning of the banking system. I am therefore encouraged by the reassurance in Mr. Harinowo's helpful statement that the authorities are cognizant of the challenge and determined to accelerate reform and restructuring of the banking sector as a priority.

Finally, I welcome the broad framework that the authorities have adopted for giving a fresh momentum to corporate restructuring. The agenda is indeed far-reaching and includes difficult challenges that have slowed reform in this area. In that context, I see improved implementation of the bankruptcy law, corporate asset recovery, and debt restructuring with the largest corporate debtors as areas of high priority. Let me also stress here that the staff provides a number of useful suggestions for action in this regard.

With these remarks, I support the proposed decision and wish the authorities success.

Mr. Zurbrugg made the following statement:

Let me start by congratulating Indonesia for its successful transition to democracy. This has been a very difficult process and, of course, serious challenges still lie ahead. Turning to the authorities' economic program, like all previous speakers, I am impressed by its comprehensiveness and its ambitious goals. Looking at the list of prior actions, the new government appears strongly committed to the program. I particularly welcome the will to forcefully address governance issues. Let me state at the outset that this Chair supports the requested new extended arrangement.

First, let me give some general remarks on past program implementation and proposed access to Fund resources.

Our past discussions on Indonesia have been characterized by a common element: program implementation in structural areas has always been lagging. While recognizing the scope of the structural measures contained in the Indonesian program was and remains enormous, resolute implementation in the structural areas is crucial for the success of the program. It is very unfortunate that the staff supplement issued yesterday appears to confirm our experiences under the previous program. A brief parenthesis on yesterday's supplement: I want to make Mr. Schlitzer's point more forceful on the usefulness of including the table of prior actions in the Staff report. Such a table would definitely help make a judgment of the authorities' efforts, particularly for the staff working in our capitals. Given the past track record in implementing structural measures, I fully agree with Mr. Milleron, that it would have been helpful to have stronger structural conditionality. We have to be very careful not to focus our future reviews of this program on mainly macroeconomic developments.

On the question of access, like Messrs. Collins, Taylor and Kiekens, I found the Staff report did not give sufficient information on why such a high access is required for this program. As I had already stressed at the time of the last augmentation, my authorities feel very strongly that the catalytic role of the Fund and the success of the program are determined more by resolute program implementation than by the financing. They are very concerned by the fact that cumulated access will temporarily climb to over 400 percent of quota, substantially exceeding the cumulative access limit and thus requiring the exceptional circumstances clause once again.

I am also concerned by the implied burden sharing between creditors that this large access entails. While I very much welcome the success of the recent CG meeting in further mobilizing multilateral and bilateral resources in support of the program, like Mr. Milleron, it is unclear to me to what degree the private sector remains involved. I also note that notwithstanding the dominance of structural issues in the program, the share of Fund financing remains very high.

On fiscal policy, the targeted deficit of 5 percent is a compromise. It supports recovery, but also signals a turn toward a more restrictive policy. The planned fiscal reform must be implemented as scheduled to strengthen tax revenues. Moreover, I hope the authorities act prudently and can resist the pressure to fix or introduce the tax-free status of certain islands. Furthermore, I welcome the fact that untargeted subsidies shall be reduced, which should help correct distortions in fuel and power prices. I welcome exempting low-income households from tariff increases. In this context, I was interested to see that the criterion for exemption is not having access to a 450-volt connection. I would be interested to know how many private households fall into this category.

Moreover, I also support the activities that are intended to reinforce the social safety net. With respect to food security, let me add that I weigh the interests of the rice consumers higher than those of the suppliers. Therefore, I hope that the support of the rice price through import tariffs will soon be abolished.

With respect to the planned wage increase in the public sector, I share the staff's concerns. I think a more gradual implementation is possible and would not be detrimental to the fight against corruption.

Turning to structural policy, this is clearly the area where the greatest challenges lie. I would only like to highlight the following points in the broad range of issues facing the authorities:

I fully agree with the staff that the lack of progress in bank and corporate restructuring is the most urgent issue. I appreciate that concrete remedies have been planned to tackle a central problem, namely making the threat of bankruptcy more credible. An important line of action is to make the judiciary more effective. I welcome the reforms - already accomplished or planned - that should strengthen the capacity of the judiciary to implement the insolvency law and help prevent corruption.

Concerning IBRA, fresh momentum is urgently needed, because IBRA is expected to make significant progress during 2000 in asset recovery. I saw the two insolvency petitions filed by IBRA in the commercial court for two cases where debtors failed to enter into good faith negotiations as a very positive step. In such cases, resolute action is needed to be credible. It is very unfortunate that the courts have rejected these requests. Is there anything the staff can add to these developments?

The outcome of IBRA's polices must be continually watched to assess whether the new strategy guarantees the expected success or whether still additional improvements are necessary. In this context, could the staff comment on whether there are lessons to be drawn from the recently failed sale of Astra? I understand that the investment community regarded this transaction as a test case for Indonesia's corporate restructuring.

Given the difficulty and enormity of IBRA's tasks, governance issues are crucial. I therefore warmly welcome the fact that first steps have been taken to preserve IBRA's independence, and increase transparency and accountability.

Finally, let me comment on the problems of the central bank. I welcome the actions to remedy the problems that have been identified by a special audit. I hope that the verification of the financial statements will not produce unfavorable surprise.

To conclude, the Indonesian authorities have challenging tasks in front of them. I wish them the energy needed to succeed in their difficult endeavor.

The staff representative from the Asia and Pacific Department noted that 450 VA represented usage of about four to five light bulbs.

Ms. Vtyurina made the following statement:

We welcome the new EFF arrangement for Indonesia although not without reservations pertaining to the underlying risks to the program. Our worries also have been aided by the fact that not all prior actions have been completed due to persisting impediments to the implementation of reforms; but we hope that they will be completed very soon. We do thank the staff and commend the authorities for designing a very comprehensive recovery program, but note that the main goals of it remain the same as in the previous EFF, especially in regards to structural reforms. Like before, the implementation of the program will depend on the authorities' commitment to the necessary changes and on the political leadership in reform implementation. The program is ambitions and we hope that it will be a success. I have a couple of specific points on a few areas of the program.

First, the fiscal side. The proposed 5 percent budget deficit seem to be appropriate for the year 2000, taking into account the need to support the recovery and, at the same time, move towards a medium-term objective of fiscal consolidation. The latter calls not only for the improvement in revenue performance, but also for a withdrawal of fiscal stimulus. However, Indonesia has never used up all of projected stimulus mostly because of under-spending on social programs. As Mr. Shaalan and Ms.Farid, we believe that it is important to assure the reaching of the targeted levels of expenditures to support the recovery and preserve social peace. Taking the above into account, two questions arise: whether there are safeguards to achieving a projected deficit, taking into account the past below-the-target performance; and whether it might be a bit premature to start withdrawing the fiscal stimulus when the country's economic position is still very vulnerable and the past deficits were not that drastically high after all. The staff comments are appreciated. In regards to the dramatic increase in the compensation to high level officials, while we agree with the staff that a more gradual approach was more appropriate, we acknowledge the authorities' intention to exercise this measure as a part of their anti-corruption strategy. These increases, however, need to be supported by the improvements in the wage structure and the administration. We agree with the staff in para 25 that the risks of this wage policy will need to be closely monitored, but the paper does not specify the ways in which this will be done. The staff comments are welcome.

The authorities' decision to maintain a flexible monetary policy is very much appropriate. As confidence improves and foreign capital flows resume, there should be room for monetary easing. Unfortunately, at present this does not seem feasible. Although recovering drastically from its lowest level, so far this year the rupiah has fallen 7.4 percent and the risk premium is rising all due to the high uncertainty about the political situation and the progress in structural reforms. While preserving a tight monetary policy is essential for controlling inflation and safeguarding the exchange rate, the still high bank lending rates are having their toll on the credit supply. At a present average rate of 23 percent the credit growth is bound to be stagnant or remain negative, as it has been at an average of -2.8 percent throughout 1999. We do hope that, with the invigoration of the reforms, there soon will be room for a further decrease in interest rates. However, at present we see a bit too optimistic the staff projections of an increase of private credit of more than 10 percent by year end. It would be helpful to learn from the staff what is behind such a rapid increase.

This brings me to the next topic, the banking sector issues. Without a doubt, considerable progress has been made in restructuring, but the remaining agenda is still very comprehensive. Despite the recapitalization and positive interest spreads, the profits are still to return and confidence to be regained. We fully concur with the steps of the proposed agenda for a completion of restructuring since most of it was inherited from the previous program. I do have one question regarding the data used for assessing the health of the banking system. As stated in the staff's supplement, the cost of bank restructuring has risen substantially from the originally estimated amount due to slower than expected pace of reforms and also because of a limited information during the period of deep crisis. Box 7 of the current staff report provides what appears to be a good overview of the health of the banking system, however, the footnote of the same box seems to disqualify the provided information by stating that "there are serious problems in the data-base and, therefore, any conclusions presented in this box should be viewed as indicative". Does this mean that there is a serious potential for a further increase in restructuring cost and how serious are the deficiencies in the data?

Finally, a remark about the assets sales by IBRA. Naturally, now this process becomes very important not only for the budgetary reasons but also because of an extreme need to return investor confidence and welcome back the foreign capital flows into the country. It is essential for the authorities to follow through with the recently taken steps to enhance the governance, oversight structure, internal controls and transparency. The first test case, a sale of Indonesia's largest car maker Astra International, seems to end in a failure. The bidder company withdrew from the process because it was not allowed to conduct due diligence. The international business community is said to perceive this sale as a big precedent; and the investors are watching very carefully to see whether the new procedures are trustworthy. It is rather disappointing that there is a repetition of the Bank Bali case. I wonder if the staff could give their views on this issue.

In conclusion, we want to wish the authorities all the success in their comprehensive agenda.

Mr. Lehmussaari made the following statement:

Indonesia continues to have serious economic challenges in the period ahead, but after the recent peaceful political transition, the new government appears to be in a better position to tackle these challenges than the previous government. The crisis in Indonesia has been the deepest and the recovery slowest in the region. Nevertheless, a fragile recovery was starting to take hold in the second half of 1999 despite the interruption of the IMF program.

In many respects, Indonesia continues to build a functioning market economy and democratic rule from scratch and the authorities are faced with a vast reform agenda. Against this background, the new extended arrangement is indispensable for supporting Indonesia's reform commitment. I can therefore support the proposed program. I also extend my acknowledgment to the Indonesian authorities and the staff for reaching agreement on the program, given all its complexities.

It goes without saying that the implementation of the program measures is the key for the stabilization effort to succeed. As the staff puts it, the implementation of this program is a multiyear task. Risks as well as rewards are high. Therefore, political consensus is critical, not only for success of the program but also, in a wider context, for maintaining the integrity of the country.

Like many other chairs, I see the fiscal policy and bank and corporate restructuring at the heart of the exercise. On monetary policy, I share the authorities' view that monetary policy should continue its supportive role. There appears to be room for further reduction in interest rates, as the inflation pressures are moderate, real interest rates are still high and fiscal policy is expected to be relatively prudent.

If the policy reform agenda is implemented promptly, the decline in risk premia will automatically work towards lower real rates. In this process, the authorities should, however, keep a close eye on the foreign exchange and inflation developments. For the monetary policy to succeed, it is likewise important that the central bank's independence is preserved and its internal controls strengthened.

On fiscal policy, the authorities should find an appropriate balance between supporting the fragile economy and, at the same time, establishing fiscal sustainability. I see the FY2000 budget as conservative, since it implies a small fiscal withdrawal in a situation where output gap is around 8 percent of GDP. In particular, the authorities' cautious stance is reasonable, not only because the general government debt is close 100 percent of GDP, but also because a substantial part of the financing is expected to stem from asset recovery and privatization. So far, the asset recovery has been, according to some estimates, extremely poor. There also appears to be a considerable difference between estimates of the fiscal cost of bank restructuring. For example, Standard and Poore's estimated it on the order of 82 percent of GDP in June 1999 versus around 60 percent in official and the staff estimates. And both estimates are multiples of that in Thailand and Korea.

I welcome the authorities' commitment to rationalize the tax system. The elimination of numerous exemptions and subsidies, as well as the strengthening of tax administration, is of critical importance. Of course, poverty-alleviation should be maintained among the top priorities.

I also see the merit in fiscal decentralization. However, as the staff rightly points out, the decentralization should not compromise the macroeconomic framework. Ensuring fiscal transparency and maintaining fiscal control and I repeat fiscal control at the general government level are crucial. Therefore, I support the authorities' willingness to first put in place proper institutional and reporting mechanisms and then proceed with the decentralization.

Like many others, I see the progress in the bank and corporate restructuring as the major factor determining the outcome of the program and the sustainability of the recovery at large. It is difficult to overestimate the importance of the successful performance of the IBRA in this context. I want to emphasize the value of establishing transparent rules for the asset sales. This would support the authorities' goal for the "quick but orderly" asset disposal, better safeguard the value of assets, and contain political interference.

I would also stress the importance of the prompt contract enforcement by the IBRA. This should not only lay the ground for a better discipline among debtors to pay back loans as agreed, but also put the pressure on the courts to implement bankruptcy legislation. The authorities' determination to decisively address the corruption in the courts clearly has bearing in this context. All this is essential for establishing the practice of good governance in Indonesian private and public sectors.

Last but not least. As the program entails considerable risks, I see frequent monitoring to be essential. This is particularly important given the extensive structural component of the program and its sensitivity to political developments.

Finally, I would like to join other speakers in thanking Mr. Neiss for many years of Fund service.

Mr. Donecker made the following statement:

Let me state from the outset that we too support the proposed decision and the policy recommendations contained in the staff appraisal. Like other speakers have pointed out, it is appropriate to reformulate the unfinished EFF-program with the newly elected government as a new program. This approach should help bolster the new authorities' commitment to the ambitious program.

Before I go into details, I would like to also take this opportunity to thank Hubert Neiss for his exemplary work while in the Fund. His dedication to his work especially in Indonesia in the past years has paid off not only in the form of a medal from the former Indonesian president or dare I say it in a new career opportunity in the Deutsche Bank. What will remain as a major achievement is the global acceptance that the IMF-medicine, advised by Mr. Neiss and supported by our Board, in South East Asia was eventually successful especially in Indonesia. A return to macroeconomic stability in Indonesia is in sight, growth is picking up, Inflation is low, interest rates are below pre-crisis levels, foreign reserves have been increased and the exchange rate has stabilized. These indicators show much progress the stabilization of the economy but major challenges lie still ahead, as the staff and many of our colleagues have already pointed out. We hope that the still fairly fragile economic recovery will also translate, into a substantial improvement of the quality of life of the Indonesian people, in particular the poorest and thus the weakest membership society.

Having said this I want to endorse the need for decisive leadership and action on the part of the authorities to implement their program. The successful transition to democracy has created a climate of consensus and willingness to change. This should help with regard to the implementation of the ambitious reform agenda. I agree with Mr. Shaalan's prudent advise that a clear prioritization and sequencing of adjustment and reform measures is needed and that such prioritization should take realistic account of the country's institutional capacity as well as political realities.

On the new program, first and foremost, like many colleagues, I would like to underscore the importance of the restructuring of the banking system and the corporate sector. This unfinished part of the reform agenda imperils not only the recovery of the whole financial sector and thereby of the whole enterprise sector, too, but it also jeopardizes the fiscal stance. Against this background, we welcome the more integrated approach of the new government emphasized in Mr. Harinowo's very helpful statement. We share the staff's view that the key for a successful restructuring lies in the hands of IBRA. We urge the authorities to desist from political interference. Last year's scandals must not happen again.

Concerning fiscal policy, we are somewhat disappointed about the envisaged widening of the fiscal deficit to 5 percent in 2000. Although there is a need for continuous fiscal stimulus, the fiscal plans appear not particularly ambitious. For example, a faster reduction of the wide range of tax exemptions would be welcome. In this context, it is doubtful whether it will be possible to implement decentralization with fiscal neutrality, as planned. Due to the high expectations at district and provincial level there will be a lot of political pressure by local groups and politicians to spent more than is available. We share the staff's concerns regarding the envisaged increase of salaries in the public sector, which could trigger similar expectations in other sectors leading to a resurgence of inflationary pressures and undermining investors' confidence.

Regarding corporate restructuring, we would like to associate ourselves with Ms. Lissakers and Mr. Sobel who see the main risk in an unsatisfactory implementation of the bankruptcy law.

Finally, Mr. Chairman, with today's decision the Fund signals trust in the authorities' commitment to their program. The level of access is quite high. With an additional 175 percent of quota, the Fund's already very substantial exposure to Indonesia will rise further. Due to the fact that the cumulative access limit is already exceeded, the exceptional circumstance clause has to be invoked again. We hope that the Indonesian authorities will show their appreciation of this continuing strong support from the Fund and the international community by an ambitious rapid implementation of their new program. We wish them and the Indonesian people much success.

Mr. Ioannou made the following statement:

Let me first thank the staff for their concise and comprehensive report and Mr. Harinowo for his very helpful statement. Indonesia has made considerable progress in emerging out of the deep crisis it suffered in late

1997. This is evidenced in part by the recovery in output, the containment of inflation, the reduction in interest rates and the appreciation of the exchange rate.

Nevertheless, progress in the areas of bank and corporate restructuring, which is essential for the sustainability of the recovery has been lagging. The subdued performance in this area, in our view, goes a long way in explaining why a return to a pre-crisis output in Indonesia is projected to take place in 2003, six years after the onset of the crisis. In this regard, we are glad to see a renewed emphasis by the authorities on the area of structural reforms and hope that the return of political stability in the country will provide the necessary impetus. Since we broadly share the staff's assessment, I will limit my remarks to a few aspects of the proposed program.

On fiscal policy, the staff argues that the planned consolidation reflects the strong pressure exerted on the government by the Parliament to reduce public debt. While the staff seems to go along with the authorities' views on this matter, we wonder if this was the staff's preferred policy course. Like Mr. Shaalan and Mr. Milleron, we are somewhat concerned about the fiscal withdrawal planned for 2000 which we are afraid it may endanger the emerging recovery. We feel that relying on structural reforms to provide an impetus to growth, is a bit premature given the problems experienced in this area in the past and the still to be tested record of the new government. As Mr. Harinowo noted, growth in 1999 was only 0.1 percent, and structural reforms, especially in the short run, are unlikely to boost the growth rate significantly. We are therefore a bit skeptical about the staff's projections of GDP growth over the medium term which we consider a bit optimistic. The staff argues that growth will be strengthened in the medium term as a result of a pick up in exports and investment, reflecting progress in bank and corporate restructuring. Looking at Table A in the staff report, the growth differential in the FY 2000 compared to the previous year is essentially due to the positive contribution of private fixed investment. For 2001, the staff assumes a sharp increase in the contribution of exports relative to the previous year. Not withstanding our reservations about the pace of restructuring, we are doubtful whether these reforms will have the envisaged results on investment and exports. This is because, corporate restructuring in the early stages will involve a prepayment of interest arrears rather than a build up in productive capacity, which in any case remains idle as reflected by the existence of a sizable output gap.

On the modalities of the planned fiscal consolidation, we note that for the most part it relies on enhanced revenues. However, for FY 2000 we note that one third of the increase in non-oil revenue will come as a result of automatic stabilizers. Given our reservations expressed above regarding the projected growth rates, we feel that the revenue target may again be rather optimistic. As other directors, we are also skeptical about the impact of fiscal decentralization on revenues. Having said this, we welcome the authorities' efforts to streamline their tax system and improve its efficiency. On the expenditure side, it is important to ensure that spending is restructured by eliminating inefficient spending and untargeted subsidies, while protecting social spending for the very needy. We also share the staff's, but also Mr. Taylor's, concerns about the sharp increase in wages for highly paid civil servants in the effort to combat corruption.

On the financing side, we notice that despite the renewed emphasis on privatizations and asset recovery, both of these items for the most part do not exhibit any noticeable increase [Table 1] over the medium term. We would appreciate some clarification on this issue by the staff.

On the issue of public debt, we agree with the need for consolidation over the medium term. Public debt as a percent of GDP has risen sharply from 25 percent in FY 96/97 to over 100 percent in FY 98/99, as a result of the restructuring of the financial sector. In light of the on going process of recapitalization, the reservations we expressed on the prospects of privatization and asset recovery over the course of the next few years, as well as on the appropriateness of GDP projections, we consider the projected decline in public debt to be rather optimistic. We feel that Table I3 is based on the assumption of a sharp reduction in the principal cost of bank restructuring and of an absence of any estimated recapitalization needs by the banking system. Could the staff elaborate a bit on how the projected declines in public debt will materialize? Furthermore, based on data in Table 1, it appears that any reduction in the ratio of public debt to GDP will involve primarily a reduction in domestic debt, not external debt- which was the primary motivation of fiscal consolidation- and which remains for the most part constant. Comments again would be welcomed.

Finally Mr. Chairman, like many other Directors, we commend the authorities for their efforts in combating corruption and improving governance. Strengthening the rule of law will enhance confidence in the judicial system, facilitate corporate and bank restructuring, and enhance the bankruptcy process. Moreover, the fair and predictable application of laws will increase confidence in the government, reduce costly rent-seeking and, more generally, enhance the working of market mechanisms. Like Ms. Lissakers and Mr. Sobel, I can report that the Netherlands is in the process of studying ways to provide technical assistance to the Attorney General. In addition, the Netherlands is in close contact with the Indonesian authorities and IMF staff, and discussing the possibility of setting up a more long-lasting judicial reform program. With these remarks, we support the proposed decision and we wish the authorities every success.

Mr. Kelkar made the following statement:

I congratulate the staff for this outstanding report prepared for the Board and I associate myself with Ms. Lissakers and Mr. Sobel to be on record about our due appreciation to Mr. Hubert Neiss for their dedication and outstanding contribution to IMF work in Asia including that of Indonesia.

In the December informal meeting the staff had informed this board that Indonesia will be approaching the Fund for a three year EFF after presentation of their budget. The new arrangement is going to replace the current extended arrangement. It would be a front loaded program built upon the achievements of the past but would also have a broad national and social support. At this juncture I would like to congratulate the authorities for having accepted a bold reform agenda. No doubt the implementation of the program will not be an easy task given the embedded challenges, but with commitment, the authorities will strike the right balance and reconcile diverse opinions and views and I hope will successfully implement the program. I fully endorse their sagacious strategy of initiating a bold program in the first year of the new government itself. I also, particularly, applaud the authorities for their policies and efforts to protect the weak and vulnerable sections of the society while implementing the reform program.

It is worth noting from Mr. Harinowo's statement that the domestic economy grew by 0.5 percent in 1999. The other domestic and external macro economic indicators have also remained under control. Even while the rupiah or the Jakarta Stock Exchange index fluctuated but it was in an environment of an overall improvement which has been perceptible and important to recovery. I am in agreement with the key objectives of the macroeconomic framework of the revised program but I also agree with the staff regarding the underlying political risks to the program in the medium term. Hence, I trust that when the authorities are implementing this program over the next three years the management and the Board will show the required flexibility regarding the specific targets and target dates mentioned in the program.

The budget is a key factor in the program in the coming year. It has been agreed to aim at a fiscal deficit target of 5 percent of GDP with a much larger level of spending than last year. This should support the economic recovery that is underway provided of course that there are no slippages. Here I would associate myself with the views expressed in Mr. Shalaan's statement regarding the risks to the fiscal stimulus and the possibility of shortfalls in the areas of social expenditures. Of course this concern has also been mentioned in the Staff report.

Coming to the tax proposals I endorse strongly the objectives of improving the tax to GDP ratio and reduce public debt. On wages policy I do see the point about increasing the salary of officials in elite positions. This could be implemented in a phased manner as suggested by the staff but then one would leave it to the judgment of the authorities who have to tackle the larger issue of rent seeking and misgovernance. However the increases could be linked to actual improvement in efficiency or productivity where it could be measured. The other measures to lift subsidies, remove tax exemptions and go in for asset sales to strengthen revenues are welcome steps. I appreciate however, that the process of fiscal decentralization may have to be implemented more gradually.

The continuity in the monetary policy and exchange policies from the earlier program is in my view the correct approach. Till date these have been helpful in keeping inflation in check and reducing exchange rate volatility. While I agree the policy should support the fiscal stimulus but it should not be allowed to jeopardize the hard earned macro economic stability relating to inflation.

It is good to see that the corporate and banking sector reform package has been revamped in view of the past experience. It had been mentioned in the December briefing that the coordinating minister would have an enhanced role in the implementation of the restructuring process. As this is the core of the program, this factor is a crucial to the success of the program. While the report has given the various measures which have to be carried out as a part of the restructuring process, I would like to know whether the role of the coordinating minister will be significantly different from the past.

There is one area where I would suggest that in the forthcoming reviews, the staff may persuade the authorities to prepare a medium-term strategy for accelerating exports, particularly manufacture exports. In preparation of such a paper, the IMF staff and the World Bank can give the required assistance. I am mentioning this because the export growth projected in this document is already somewhat sluggish and any setback in this regard will have serious implications. Hence, I agree with Mr. Kiekens that an early appreciation of rupiya can be potentially problematic and the authorities will need to be vigilant about this.

Having said this at this stage I would only welcome what the authorities have set out to do. It is a difficult road ahead and in time one will see and also review where the program is going.

Today, I would like to support Indonesia's request for an extended arrangement and wish the authorities success in the difficult tasks ahead.

Mr. Fenton made the following statement:

We are very please to have this excellent set of documents before the Board today. The last 6 months were precarious ones in many respects for

Indonesia. And the staff and the authorities deserve much credit for not only holding things together, but producing such a promising framework for addressing Indonesia's problems. Nevertheless, we are cognizant that, difficult as this was, it was probably the easier part of the process. Now comes the task of implementing this program, most likely in the face of strong opposition from entrenched vested interests. Accordingly, the importance of good governance in the period ahead cannot be over-emphasized. If the authorities implement this program in a firm determined way, Indonesia can work its way out of its problems, if the authorities fail to implement the key elements of this program, Indonesia will be condemned to years of muddling along.

The key elements of the program have already been covered by other speakers so I won't discuss them in detail. But from our perspective two areas are especially important: governance, as I just indicated, (here I would like to associate myself with the comments by Mr. Collins and Mr. Taylor in their statement); and financial and corporate restructuring (here I would like to associate my self with the suggestions made by Ms. Lissakers and Mr. Sobel in their statement, particularly with respect to IBRA) . Whether the targets for loan collection and asset recovery are achieved, or not, will be a significant indicator of how vigorously and effectively the authorities are pursuing corporate and financial sector reform. We would like to emphasize that, in our view, lack of progress on privatization and asset sales would not justify a request for additional IMF resources.

With respect to fiscal policy, we support medium-term consolidation, but this must be balanced in the short term with the need for an appropriately stimulative policy environment. Within this context, we would urge the authorities to pay particular attention to the consequences of their actions for the poorest members of society. On the issue of fiscal decentralization, we wish to associate ourselves with the position of Mr. Toyama

We welcome the staff's commitment to strong monitoring of the program. We would also favor sending a strong signal to the Indonesian authorities that slippages on the fiscal plan will not be filled with additional IMF resources.

Finally, Mr. Chairman, I would like to express this chair's deep appreciation to Mr. Neiss for his very important contribution to the work of the Fund . His wealth of experience and profound personal commitment were particularly important to Indonesia in recent months.

Mr. Kudiwu made the following statement:

Like previous speakers, we welcome the adoption of a new economic program by the Indonesian authorities, which aims at reinvigorating the economic reform, accelerating the reform agenda, and enhancing governance. Like many other speakers, we believe that it is important for the authorities to build on the progress achieved so far and to intensify efforts to improve employment opportunities, reduce poverty, and assure equality of chance to the Indonesian population. We also share the view that with a new economic program, the country is well posted to join its neighbors in a strong recovery process. However, while the proposed program involves already many risks, it is our expectation that the ongoing political tensions in the country will be addressed as soon as possible and in a peaceful manner.

This being said, our remarks will focus on two areas for emphasis, namely fiscal sector and structural reforms.

On the fiscal sector, we are pleased to note that fiscal policy is expected to remain a key component of the program. In this regard, the authorities' intention to strike a balance between supporting the economic recovery and starting the process of reducing government debt is welcome. Moreover, like Mr. Shaalan and Ms. Farid, we see merit in the wide-ranging tax reform program envisaged under the FY2000 budget.

On public spending issues, we hope that at around 30 percent of the overall social spending projected in FY 2000, the social safety net programs are well targeted. Also, a successful implementation of fiscal decentralization in 2001 is critical. However, given the limited time available for its preparation, and like other speakers, we would like to encourage the authorities to proceed carefully with its implementation.

To ensure credibility, bank restructuring remains a key aspect of the overall program and needs to be accelerated. We welcome the progress made during the later part of 1999 in most aspects of the bank restructuring program, and in particular, the reduction of their number from 238 as of June 1997 to 165 as of September 1999. Could the staff provide us with some information on social costs involved by the closures and mergers of banks?

The corporate restructuring constitutes another key component of the program, which will need to be addressed without delay. We welcome the efforts being made to move corporate restructuring ahead, in order to restore credit flows that are needed to support the economic recovery. The government's commitment to tackle the bankruptcy reform problem and enhance the governance framework in judiciary is reassuring.

Finally, in light of the positive achievements accomplished in dealing with the financial crisis and the firm commitment of the new government to the reform process, we have no difficulty in supporting the authorities' request for a new extended arrangement that could help the country to foster international confidence in Indonesia's reforms and to gather additional financial support. As stressed in Mr. Morais' statement, it is essential that the authorities translate their commitments into action.

With these remarks, we wish the Indonesian authorities every success in their future endeavors.

Mr. Pascual made the following statement:

From the start I would like to commend the staff for the enormous work they have done to prepare a most needed new program with Indonesia. I would also like to congratulate the authorities for their efforts and for their will to tackle a very complex situation Indonesia is living now. I think, nevertheless, that this is the only way out.

I support the new extended arrangement, and the associated increase in access. I believe, however, that the program does entail great risks for the Fund, and I am not thinking only on the resources of this Institution. In fact, I believe that the greater risks are for our image. Indonesia is an important point of reference for the entire financial community on how this Institution deals with the causes entrenched at the root of the recent crisis. It is essential, in this light, to proceed expeditiously to remove structural and institutional hurdles that have been impairing the effective recovery of the economy and the restoration of confidence in the markets. Governance is a major issue in this program. I applaud the authorities and the staff for considering so. The international community is expecting a sweeping change that would ensure that financial support is not wasted.

I think that the program is comprehensive enough to achieve these goals. However, the tasks ahead are enormous, especially in a context of unrest and political change. Under these circumstances, I welcome the enhanced monitoring included in the program, although, like Messrs. Collins and Taylor, I would prefer the establishment of structural reform targets within the performance review criteria.

As a general comment, I would also prefer a more detailed description of the private sector involvement in sharing the financial burden. I appreciate the supplementary information the staff has provided, but it still remains unclear.

Policy mix seems appropriate. Fiscal policy, while constrained by the need of long-term sustainability, must support the nascent recovery. Monetary and exchange rate policies should be kept on focusing price and exchange rate stability. However, I agree with Mr. Milleron that several risks make a very cautious monitoring of the program warranted. Debt dynamics, fiscal decentralization programs and bank and corporate restructuring introduce a great deal of distortionary interference that could seriously affect the outcome

> of an otherwise very rigorous policy mix. In particular, I am concerned with the distortions that bank and corporate restructuring are imposing in the transmission mechanism of monetary policy. I believe that for a long time bank managers are not going to be willing to take new financial risks other than those guaranteed or collateralized. This means almost for sure a credit crunch. Being so, I tend to believe that the forecasted ten percent increase in credit to the private sector is wishful thinking.
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> It is very difficult not to agree with most prescriptions included in the program of structural reforms and bank and corporate restructuring. Therefore, I will not comment on the specific measures.
>
> I would just like to stress the importance of implementing the program in a timely fashion. A bold, comprehensive and coherent strategy is crucial for these reforms to have limited distorting consequences on the economy and positive effects in the recovery. I welcome in this light the establishment of the Financial Sector Policy Committee. This would help to concentrate responsibility and decision-making power providing guidance and thrust to this difficult process. By the same token, IBRA's powers must be enhanced and its independence guaranteed. There cannot be much progress if major actors are engaged in continuous struggles against corruption, or solving jurisdictional conflicts that might be solved out of court. But again, I believe the authorities are aware of all the risks being taken while managing so complex a political situation.
>
> Under these circumstances, I can only conclude conveying the authorities my best wishes and all my support to face the difficult times ahead.

Mr. Hendrick noted that for Indonesia not only extraordinary balance of payments needs existed to support a standing arrangement, but also structural reforms were needed for longer periods. Additionally, the issue of ownership was not the only explanation for the new arrangement.

He reiterated, that while the authorities had announced the upper end of the range for GDP and inflation numbers, the staff had carried out their analysis using the lower range. He would appreciate that, in the future, ranges were not used, but only numbers consistent with those used in the financial programming.

The Deputy Director of the Asia and Pacific Department made the following additional statement:

> On the private sector role in providing financing, there is no doubt that the private sector has played and is expected to continue playing a major role as corporate restructuring gains momentum. When comparing the London Club with the Paris Club, there is an additional way in which the private sector could play a role; be it through a London Club scheduling or through another

modality. But the minimum amount that the staff would expect from the private sector is supplied in Table 2 of the supplement to the staff report.

On IBRA's petitions to have ad hoc judges assigned to some cases, it is the assessment of the Legal Department that the reasons given for turning those petitions down could be spurious and more facts needed to be found out. While one petition had been turned down for technical reasons, the other one was for procedural reasons. However, the President of Indonesia has announced that he will replace the judges in the Supreme Court in due course. It seems to the staff that such a change may be necessary to accomplish the objectives of the bankruptcy law. In any case, the commercial court is not subject to the discretion of the government or of parliament. In that regard, there is no doubt that the resistance to the sale of Astra has been based on vested interests. That related to the general question of the risks to IBRA's recovery. A special meeting of shareholders would be called next week and the expectation is that either a management change will take place or that the current management will allow the process of selling of IBRA's 45 percent shares to move forward. The way in which that is resolved will show up the future risks to IBRA's recovery and the whole program of corporate restructuring, as well as IBRA's independence.

On the staff's assessment of the recent wage increases, the sense is that the average wage to GDP ratio is at a level where any further increases should be treated cautiously. Future changes should be directed at the wage structure and carried out in tandem with civil service reform and the anti-corruption drive. A large gap exists at present in the upper echelon which needs to be closed.

While the banking data in the report is largely based on unaudited data, surprises in recapitalization costs should not be expected since most bank audits have been completed. All the private banks have been audited and only BNI, two other smaller state banks and some of the banks-taken-over remain. Therefore, the staff does not expect surprises in bank recapitalization costs, such as encountered over the last twelve to eighteen months.

On the growth projections and whether the fiscal stimulus will be sufficient, the staff had supplied ranges in a number of programs, and also in Indonesia in the past. The reason is that the staff are not able to predict a specific number currently, and therefore do not want to inform the Board that growth will be 4.5 percent. The range was narrow, and its significance is to indicate that a lot of uncertainty still exists and that the program needs to be looked at carefully as it is implemented and adapted to resolve this uncertainty. For example if more stimulus is needed, the staff have been quick to respond in the other Asian programs, and will act in a similar manner in the case of Indonesia, if needed.

The staff's quantitative analysis shows that the reduction in the public debt was due to macroeconomic factors, such as accelerating growth, maintaining low inflation, asset recovery and fiscal consolidation. However, over a sustained period, Indonesia will not be able to keep macrostability and high growth, if it is not able to make progress on corporate restructuring and asset recovery.

In the Asian countries in general, credit has been slow to pick up, because only a small number of credit worthy borrowers exist. And until corporate restructuring yields a base of credit worthy borrowers this situation will not change. As regards the link between exports and credit, the principal constraint to a recovery in exports could be the lack of available trade finance.

Mr. Harinowo made the following concluding remarks:

I have carefully listened to statements by the Directors and the staff, and am profoundly impressed by the overwhelming support received. Most of the comments have focused on fiscal policy, progress in banking restructuring and the prospect of the external position. The staff have given excellent clarifications of those issues and I will only add a few points.

On the question of whether Bank Mandiri will start turning profits, the staff has provided some answers. Recently a public statement was made by the president of Bank Mandiri that the bank is projecting a profit this year in the amount of almost one trillion rupiah, which is significant. At the same time Bank Mandiri is also planning an IPO to be completed this year or next year. This IPO will address the issue of the share of state banks in the overall banking systems.

Secondly, on the progress of asset sales by IBRA, we have learned that progress has been made with two major sales. The IPO of one bank and the sale of shares in Astra. Additionally, four foreign companies have indicated their interest in buying shares. The chairman of IBRA confirmed today that IBRA will send letters to the interested bidders and, he also indicated that, at the latest, the sales have to be completed by March 25. IBRA will provide ample time for the investors to carry out a due diligence process. On the IPO of Bank BCA, progress continues to be made. In general, a top priority is to transform the banking system from family owned institutions to publicly owned entities.

On the issue of decentralization, my government has made serious efforts in striking a fine balance between the need to safeguard fiscal integrity and the need to contain the centrifugal forces. The staff has helped my authorities in indicating the risk of too hastened an approach. Therefore, my authorities are fully aware of this issue and are trying their best to reach the most optimal solutions within all these constraints.

On the issue of the magnitude of the reforms, in my statement my authorities indicated that they will steadfastly and unfailingly pursue the reform program. Some Directors have indicated how immense the program is. It is true that the new government has a long list of actions which they need to accomplish in order to establish themselves as credible and well supported. My authorities confirm their commitment to full implementation of the program, however, some delays in several areas may be unavoidable.

Finally, Mr. Chairman, I once again convey my authorities' deep appreciation to the Board, management and the staff for the support extended to us. I will convey all invaluable advice and suggestions to my authorities. And to Mr. Neiss, who will be leaving the Fund shortly, I express our deep appreciation for his role in lifting Indonesia out of the crisis.

The Acting Chairman said farewell to Hubert Neiss and thanked him, on behalf of management, staff and colleagues, for his devotion to the Fund, particularly during his work on Indonesia and the Asian crisis. He noted that Hubert Neiss had been one of the earliest staff members to promote fiscal expansion in the Asian countries, and to emphasize the need to move ahead with corporate debt restructuring. Mr. Neiss's devotion to Indonesia and to the Fund was recognized soon, and it was because of him that the Fund had remained popular in Indonesia.

The Acting Chairman made the following summing up:

Executive Directors supported the authorities' request for a new extended arrangement. They commended the recently elected Indonesian government for adopting a comprehensive and ambitious economic reform program which, if fully implemented, would lay the foundations for sustained economic recovery. In particular, Directors strongly welcomed measures aimed at improving transparency and enhancing the governance of key economic institutions. They noted that the large number of prior actions already completed has underscored the authorities' strong commitment to the adjustment program and to the implementation of the core elements of their structural reform agenda.

Directors observed that macroeconomic policies had room to become more supportive of the emerging recovery. Interest rates remained high in real terms; as confidence improves, and risk premia fall, interest rates could be guided down further. In the view of most Directors, the proposed fiscal deficit of 5 percent of GDP envisaged for FY 2000, strikes an appropriate balance between supporting the recovery and starting fiscal consolidation, but some would prefer a larger degree of fiscal stimulus. Directors welcomed the expenditure reforms aimed at better targeting poverty, and emphasized the importance of tax reform measures aimed at fully restoring Indonesia's tax base and improving the efficiency and equity of the tax system so as to enhance revenue performance over the medium term.

However, a number of risks in the implementation of fiscal policy were seen, which needed to be skillfully addressed to preserve social stability. First, and perhaps most importantly, fiscal decentralization would need to be carefully managed to meet regional aspirations while maintaining fiscal neutrality. Second, while welcoming the planned phased reduction in the fuel and power subsidies, they emphasized that these adjustments should be accompanied by effective targeting mechanisms to help protect low income households. Third, they cautioned that public sector wage policy harbored some risks, and proposed that the task of narrowing the remuneration gap with the private sector be tackled in a multi-year framework, in tandem with civil service reform and anti-corruption efforts.

Directors noted that the delay in restructuring and recapitalizing state banks had been costly but welcomed recent progress, particularly the recapitalization of Bank Mandiri. They cautioned that the planned management change in the other major state banks needed to be speedily completed so that their restructuring and recapitalization could finally move ahead amidst conditions of improved governance.

Directors considered that improving bank supervision remains a key challenge. In this context, they welcomed the publication of the audit of Bank Indonesia, and urged full implementation of its recommendations. They also looked forward to the newly independent Bank Indonesia setting the future standard for accountability and transparency within financial institutions in Indonesia.

Directors welcomed the strengthened framework for loan recovery and corporate debt restructuring. Given the Indonesia Bank Restructuring Agency's (IBRA) central role in both these tasks, its independence from political interests is a sine qua non for safeguarding governance and delivering results. Providing IBRA with clear authority to engage in debt reduction was also judged to be very helpful. The greater role of the Jakarta Initiative Task Force, the ability of the Attorney General to initiate court cases, and the referral powers of the Financial Sector Policy Committee, were considered innovations that could help impart much needed momentum to corporate restructuring, and should be fully implemented as soon as possible. However, Directors noted that risks remained from the judiciary's implementation of the bankruptcy law, which underscores the need for full implementation of the anti-corruption initiatives under the program.

Directors commended the authorities for the measures in the program aimed at increasing transparency and enhancing corporate governance. In particular, they welcomed the initiatives designed to identify extra-budgetary resources and quasi-fiscal activities, and to bring them under government control and audit, including those related to the military. They noted the publication of audits of four key state enterprises and urged the authorities to implement fully programs of corrective action in these enterprises as soon as possible.

Directors welcomed the breadth of the structural reforms in the program, including the privatization, agriculture, and environmental measures. They also welcomed the authorities' plans for restructuring the rice and sugar sectors; these efforts are key in improving efficiency and productivity in agriculture, and also strike at the heart of concerns over poverty.

A few Directors referred to the commitments made by members of the CGI in their recent meeting in Jakarta which, together with continued support from bilateral and other creditors, should ensure that the program is fully financed.

Directors noted that the authorities are embarking on ambitious and comprehensive reform efforts. They considered that close monitoring of the program will be required during its first year, so as to ensure that the Fundamental objectives of the program are achieved. They endorsed the envisaged bi-monthly reviews in 2000.

Directors welcomed the close collaboration between the authorities, the Fund, the World Bank, and Asian Development Bank in formulating key elements of the program.

The Executive Board took the following decision:

1. Indonesia has requested an Extended Arrangement from the Fund, in an amount equivalent to SDR 3,638.0 million, through December 31, 2002.

2. The Fund approves the Extended Arrangement set forth in EBS/00/8, Supplement 1.

3. The Fund waives the limitation in Article V, Section 3(b)(iii) of the Articles of Agreement. (EBS/00/8, 1/20/00)

Decision No. 12136-(00/12), adopted
February 4, 2000

DECISIONS TAKEN SINCE PREVIOUS BOARD MEETING

The following decisions were adopted by the Executive Board without meeting in the period between EBM/00/11 (2/2/00) and EBM/00/12 (2/4/00).

4. EXECUTIVE BOARD TRAVEL

Travel by an Executive Director as set forth in EBAM/00/17 (2/2/00), by Advisors to Executive Directors as set forth in EBAM/99/171, Supplement 1 (2/1/00), EBAM/00/9, Supplement 2 (2/1/00), and EBAM/00/17 (2/2/00), and by an Assistant to Executive Director as set forth in EBAM/00/17 (2/2/00) is approved.

5. TRAVEL BY MANAGING DIRECTOR

Travel by the Managing Director as set forth in EBAP/00/12 (2/2/00) is approved.

APPROVAL: August 17, 2001

SHAILENDRA J. ANJARIA
Secretary