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Statement by Mr. Zamani and Mr. Zubir on
A Methodology for Exchange Rate Assessments and Its
Application in Fund Surveillance over Major Industrial Countries
(Preliminary)
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The staff paper on this subject do provide a useful insight as to how the Fund goes about in carrying out its surveillance of exchange rates of the major industrial countries. However, I do have a number of thoughts and concerns after reading this paper, and I will like to raise them according to the order of the issues identified by staff for discussion as listed on page 47 of the paper.

1. At this stage of the Fund's existence, there should no longer be any doubt that the Fund should indeed continue to strengthen its analysis of exchange market developments as part of its mandate for the surveillance of the global economy. The question that remains is how this mandate can be done effectively and efficiently. The task is indeed made more difficult by the nature of exchange rates themselves. As recent events have shown, exchange rates are no longer influenced by a country's economic fundamentals alone, but also by factors which are not easy to define and quantify. For this reason, I can agree that it is indeed becoming difficult to be very precise in identifying "equilibrium values" for <u>any</u> exchange rate, and that, for this reason, it is important for the Fund to identify circumstances in which <u>any</u> exchange rate can become substantially inconsistent with its medium-run fundamentals.

2. I can agree that the currencies of the major industrial countries are of systemic importance. However, this is not and should not be the justifying reason for the Fund to focus its exchange rate surveillance and resources largely on these countries. There are two inter-related reasons for my stand. <u>First</u>, there are already in existence numerous academic, monetary and multilateral bodies focusing their attention on the same issues for these countries. It may be more efficient use of resources for the Fund to devise means to regularly consult and incorporate their views, rather then to start from scratch and re-invent the wheel. In-house research at the Fund for these major countries should then be supplementary, rather then basic. It must be borne in mind that, earlier this year, staff themselves had admitted that in view of the increasing workload, there is a pressing need to prioritize the Fund's limited

resources. Second, given that these major industrial countries already have tremendous private and public sector resources devoted to research in every aspect of their economy, including their exchange rates, it would be more prudent for the Fund to allocate a greater share of its surveillance and research resources to the benefit of the greater number of its members who do not have and cannot afford such facilities. Taken in this context, the staff should adapt the CGER framework so that it can be usefully applied to a broader set of Fund members. In this respect, staff clarifications would be welcome as to (a) exactly which countries is the CGER presently applied to; and (b) the reasons as to why this CGER framework cannot be applied to countries who have no access to international financial markets.

3. Staff should be wary about succumbing to the academic seduction of building esoteric research models with no actual real life applications. It must always be borne in mind that the IMF is a front-line multilateral institution in the maintenance of international monetary stability. Policy-makers rightly expect the Fund to provide them with realistic advice and workable solutions to the difficulties that they confront. While medium-run equilibrium may be of some importance, it is equally if not more important for policy-makers to address their immediate situation. Staff may want to consider a more active working relationship with renown monetary research institutions and think-tanks rather then do everything in-house. Their main concern should be translating existing research into realistic policy advice.

4. I can definitely agree that appropriate policy responses to crisis situations should be addressed on a case-by-case basis, as no two situations are exactly similar, even if they occur within the same region, or the countries involved are at roughly the same stage of economic development. The challenge is for the IMF to inform and educate fund managers on this reality. Perhaps the Fund might want to consider opening its courses and seminars at the IMF Institute to market participants, on the condition they themselves pay for the full costs of the training received.

5. I would like to highlight the real underlying issue here: when and how should the Fund communicate its concern about certain exchange rate movements or the unsustainability of an exchange rate arrangement without itself sparking off severe market over-reaction. The answer is certainly not easy, as the Fund is still grappling with this issue despite being in existence for over half a century. A possible solution might be in communicating the concerns of the Fund staff and Executive Board to a closed-door forum of high level monetary officials from an affected region. The main idea is to allow peer pressure to persuade the economy (ies) concerned to undertake the necessary corrective measures. I believe this has already been done to a certain extant with the G-7, and has already been advocated to the East Asian region.

Finally, I would like to express my disappointment on reading footnote 5 on page 6 of the staff paper, that the much awaited work on various immediate exchange rate issues for developing countries will likely be completed later rather then sooner. I am given to understand that calls for these papers have been made since early 1995, soon after the start of the Mexican crisis. I would like to urge staff and management to give these issues greater priority in the forthcoming work program.