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بعنوان

The Role of International Organizations in solving Global Financial crisis

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مستخلص:

توجد أهمية بالغة لدور القطاع المالي في الاستقرار المالي والاقتصادي والتنمية الاقتصادية علي كل من المستوي الدولي والمحلي. فعلي المستوي الدولي نجد أن العلاقات بين الأنظمة المالية في الدول المختلفة بسبب حركة رؤوس الأموال والاتفاقيات التجارية تجعل الأزمة المالية تنتقل من دولة إلي أخري. أو بالتالي قد تثير مشاكل مالية علي أقل تقدير. أما علي المستوي المحلي فمن المعروف أن عدم الاستقرار المالي يعيق التنمية الاقتصادية ويؤدي إلي مشاكل في تنمية القطاع الحقيقي وينتج عن ذلك فوضي تؤثر علي الوضع الاقتصادي والاجتماعي. بالنسبة للسودان فعلى الرغم من أن القطاع المالي يمثل نسبة ضئيلة من الناتج المحلي إلا أن أهميته تنبع من النمو المتوقع له ودوره المتوقع في تخفيف الفقر عن طريق تفعيل احد مكونات القطاع المالي (قطاع التمويل الأصغر). والسودان باعتباره عضو في المنظمات الدولية يقوم بالمشاركة الاختيارية في البرامج المقدمة وتطبيق كل الالتزامات المطلوبة فعلي سبيل المثال لا الحصر المشاركة في برنامج تقييم القطاع المالي الذي بدأ في العام 2004 وانتهي في 2005 كما قبل الالتزام بالمادة الثامنة قسم 2–3 والخاصة بحرية التحويل للمعاملات الدولية. مما يدل علي تعاون الأعضاء في المنظمات الدولية واعتماد الدول ذات الدخل المنخفض علي دعم وخبرة المنظمات الدولية. من هنا جاء التساؤل حول الدور المناط بهذه المنظمات الدولية في مدى مساعدتها للدول بالعون المالي والدعم الفني لمراقبة قطاعها المالي ودراسته لمعرفة مواطن الضعف وتقوية قدرته علي مجابهة الأزمات وتخطيها ليكون قطاع كفؤ ومستقر. ومدى قيامها بالعمل تجاه قيام نظام مالي دولي متناغم ومستقر..

الأزمة المالية الحالية (2008) تستدعي النظر في كل السبل لتجنب تداعياتها. ولذلك تم النظر إلي دور المنظمات الدولية والتركيز هنا علي كل من صندوق النقد الدولي والبنك الدولي حيث لهاتين المنظمتين قدرات عالية من حيث القدرة المالية والكفاءة العالية لمنسوبيها والمساندة الدولية، والهدف من تناول هذا الموضوع هو معرفة مدى قيام المنظمات بأحد أهم مهامها وهو تشجيع الاستقرار المالي الوطني والعالمي وذلك من خلال المراقبة وتقديم العون المالي والفني، حيث يركز نظام المراقبة علي مواطن الضعف التي تساعد علي حدوث الأزمات المالية وتقوية القدرات لمواجهتها. ولذلك تم دراسة الأزمات المالية ومصادرها وأنواعها ونظريتها وملخص لأهم الأزمات المالية.

عند تأسيس كل من صندوق النقد الدولي والبنك الدولي في عام 1944 كان من أهم المهام الموكلة لهما المراقبة التي تتمثل في قيام البنك بأنشطة تمنع الأزمات المالية من خلال السياسات الفعالة ومراقبة تطبيقها وللتأكد من أنها تتماشى مع الظروف المالية والاقتصادية والسياسية. منذ بداية التسعينيات من القرن الماضي ظهرت كثير من الأزمات والمشاكل المالية والظروف الدولية مما حدا بالمنظمات الدولية وضع برامج لتقييم ومراقبة القطاع المالي للدول الأعضاء وكان الاشتراك فيه تطوعي حيث قام صندوق النقد الدولي بالتعاون مع البنك الدولي وعدة منظمات أخرى بتقديم عدة برامج للقيام بالدور المناط به. من أهم هذه البرامج برنامج لتقييم القطاع المالي الذي نتج من الأزمة المالية الآسيوية وبرنامج لقياس مؤشرات السلامة المالية وتقييم لمدى تطبيق مبادئ بازل الأساسية للرقابة علي المصارف.

عند دراسة دور المنظمتين الدوليتين كانت هناك دلائل علي عدم قدرتهما علي مساعدة الدول لتجنب الأزمات المالية ولوضع البرامج والسياسات التي تساعد علي مواجهتها. وإن حدوث الأزمات والمشاكل المالية المتلاحقة يدل علي عدم تحقيق الأهداف المطلوبة مما يعني أن البرامج التي وضعت تحتاج إلي إعادة النظر فيها والتركيز علي برامج وسياسات متطورة حسب واقع الحال الاقتصادي وتطوره، وتكون هناك كثيرا من الشفافية في نشر نتائج تطبيق البرامج والسياسات لمعرفة جدواها وعيوبها. كما إنه من الملاحظ أن المنظمات الدولية تضغط علي الدول الفقيرة أكثر من الدول الغنية التي هي أساس الأزمات المالية العالمية التي تؤثر عليها وعلي الدول الفقيرة.

Introduction

The importance of the financial sector in any economy is a key area that needs to be addressed so as to design policies to foster the financial sector stability and development at local level and global level. The international turmoil in the last few months and the threat of the crush of the world financial system and the threat of a world wide economic recession has provoked much reflection and analysis. This reflection has to consider the ways to strengthen both the individual country financial system as well as the global one. The causes of this turmoil were the theme in which all concerned beginning from financial analyst economist, political analyst, international agencies and of course government all round the world are working on. The literature of the crisis has all agreed that this was the result of the failure of the idea that the markets could regulate themselves. The international organizations, national authorities, and the private sector, are working on a series of initiatives intended not only to save the day but to find measures that contribute to a more stable and efficient financial system, and toward better preparedness to address future systemic problems.

Importance of the presentation

The importance of this presentation stems from the importance of the stability of financial system to both the global financial system and global economy and the individual country financial system and economy. The global importance results from the Contagion Effects since a country's financial system is linked to other countries' systems through capital market flows (Financial Markets Correlation*)* and bilateral trade (trade Spillovers), the occurrence of financial crises in other countries could trigger a financial crisis or distress at the domestic level. Also the magnitude and mobility of international capital flow between the different countries made it increasingly important to have a sound domestic financial system as a way to build up resilience to capital flow volatility. On the national level it is a known fact that financial instability harm economic growth and causes major disruption of real sector development thus any weakness can trigger economic turmoil and amplify the effect of the adverse shock on the economy with sever economic and social consequences.

For the Sudan although the financial sector is only a small fraction of GDP the development of and the stability of the financial sector is important because of the potential growth of this sector and for the aim to reduce poverty through the strengthening of the growing financial system and the activation of one of the component of the financial system microfinance. Sudan has to rely on International organizations, since as member country it has always participated voluntary in the program and abided by the mandate of

these organization for example participating in Financial sector Assessment Program and the application of article VIII section 2-3-and 4 on 2003 and was conclude in 2007 in which the Sudan maintain an exchange system free of restriction on the making of payment transfers for international transactions.

Objective of the presentation

This presentation aims at looking into the role played by international organization in helping the countries to monitor their national financial system identify its weakness and strength and its vulnerabilities, to enhance the country diagnostics skill and its crisis preventory role. Also to examine how international organizations help to promote more harmonization and international integration of the world financial systems . The role of International Monetary Fund (IMF) and the World Bank (WB) the two renowned international organizations in particular will be extensively deliberate as they jointly funded programs and proposed policies in which most of its member accepted and participated.

The question to be asked

Did the international organizations provided guidance on approaches, methodologies that succeed in helping countries to evade financial crisis?

Hypothesis:

We assume that International organizations with their ample financial resources, high caliber staff and international support should provide programs which:

a- Contribute to a more stable and efficient financial system and better preparedness to address any future systematic problems

b- Strengthen international financial system to face international financial turmoil

Organization of the Presentation:

The presentation is divided into two parts and a conclusion as follows:

The first part

This part represent a review of the financial crisis that has the impact on the financial systems of the world since the nineties of the last century. The definition of financial crisis its theories, reasons and consequences are given. A detail explanation of the Asian crisis which stimulated IMF to taken action is given. The 2008 financial crisis is also explained showing its reasons the consequences and the remedies taken by each individual country and the suggestion of the international organizations for a way out of the crisis, the way to avoid its consequences and to prevent of its recurrence.

The second part

This part present an explanation of the role of International Monetary Fund ((IMF) and the World Bank in helping its member countries, by providing technical assistance, assessment programs and reforms suggestions which was a part of their mandate in 1944. A special emphasis on programs, which are joint effort with other international organization, are reviewed three of these program were chosen for their relevance to the present crisis. First the joint program of IMF and World Bank program for assessing the financial sector. Second the guide for financial soundness that was coordinated by the IMF with the support of the World bank , the Organization for Economic Co-operation and Development, Bank for International settlement, and the European central bank. The third program is the assessment of compliance with Basel Core principle for effective banking supervision.

The conclusion:

A discussion of the effectiveness of the programs, methodologies and technical assistance was presented . The discussion resulted in several recommendations

The first part

Financial crisis

The Wikipedia (Internet encyclopidia) explained that the term financial crisis is applied broadly to a variety of situations in which some financial institutions or assets suddenly lose a large part of their value. Most of the financial crises were associated with banking panics, and many recessions coincided with these panics. Other situations that are often called financial crises include stock market crashes and the bursting of other financial bubbles, currency crises, and sovereign defaults. Many economists have offered theories about how financial crises develop and how they could be prevented. The literature proposed three theories for financial crisis **:** World system recurrent major depressions in the world economy at the pace of 20 and 50 years is cyclic. Minsky theory this theory assumes that financial fragility is a typical feature of any capitalist economy that leads to a higher risk and thus to financial crisis. Coordination games are mathematical approaches to modeling financial crises. There are four types of financial crisis are Banking crises when a bank suffers a sudden rush of withdrawals by depositors, this is called a bank run. The second is Speculative bubbles and crashes economists say that a financial assets exhibit a bubble when its price exceed the present value of future income that would be received at its maturity. Currency crises when a country that maintains a fixed rate is suddenly forced to devalue its currency because of speculative attack. Wider economic crises a downturn in economic growth lasting several quarters or more is usually called a

recession. http://en.wikipedia.org/wiki/Maturity_(finance)

The causes and consequences of financial crisis can be summarized as follows: Strategic complementarities in financial markets: It is often observed that successful investment requires each investor in a financial market to guess what other investors will do. Economists call it an incentive to mimic the strategies of others' strategic complementarily therefore, financial crises are sometimes viewed as a vicious circle in which investors shun some institution or asset because they expect others to do so. Leverage: means borrowing to finance investments, is frequently cited as a

contributor to financial crises. When a financial institution (or an individual) invests its own money, it can, in the very worst case, lose its own money. But when it borrows in order to invest more, it can potentially earn more from its investment, but it can also lose more than all it has. Asset-liability mismatch another factor believed to contribute to financial crises is asset-liability mismatch, a situation in which the risks associated with an institution's debts and assets are not appropriately aligned. Regulatory failures Governments have attempted to eliminate or mitigate financial crises by regulating the financial sector. Fraud has played a role in the collapse of some financial institutions, when companies have attracted depositors with misleading claims about their investment strategies, or have embezzled the resulting income. Œcopathy a Swedish psychologist Torbjorn K A Eliazon have proposed a new psychological concept of œcopathy, when economic smartness or greed crosses the borders to an extreme blinding speed that is an economic understanding without moral values, where the word "more" becomes a central existential position.

Contagion refers to the idea that financial crises may spread from one institution to another, such as when a bank run spreads from a few banks to many others, or from one country to another, as when currency crises, sovereign defaults, or stock market crashes spread across countries. Recessionary effects some financial crises have little effect outside of the financial sector, but other crises are believed to have played a role in decreasing growth in the rest of the economy.

Table 1

A short list of some major financial crises since 20th century

Date	Event
1910	Shanghai rubber stock market crisis
1980	Latin American debt crisis, beginning in Mexico
1989-91	United States Savings & Loan crisis
1990	Collapse of the Japanese asset price bubble

1992-93	Speculative attacks on currencies in the European Exchange Rate Mechanism
1994-95	1994 economic crisis in Mexico: speculative attack and default on Mexican debt
1997-98	Asian Financial Crisis: devaluations and banking
1998	Russian financial crisis: devaluation of the ruble and default on Russian debt
2001-02	Argentine economic crisis (1999-2002): breakdown of banking system
2008	Global financial crisis in USA, Europe: spread of the U.S. sub-prime mortgage crisis

Table2

A list of some episodes of financial instability in the 1990's

Date	**Event**
1990	Collapse of market liquidity and issuance of Swedish Commercial papers
1990-91	Norwegian banking crisis following loan losses
1991-92	Finnish banking crisis following loan losses
1991-92	Swedish banking crisis following loan losses
1992-96	Japanese banking crisis following loan losses
1992	ECU bond market collapse
1992-93	ERM crisis Speculative attacks on currencies
1995	Mexico crisis default on Mexican debt
1997	Asian Financial Crisis: devaluations and banking
1998	Russian financial crisis: currency devaluation

Asian Financial crisis

The basic diagnosis was that East Asia had exposed itself to financial chaos because its financial systems were riddled by insider dealing, corruption, and weak corporate governance. Asian crisis was created not by market psychology or technology, but by policies that distorted incentives within the lender-borrower relationship. The resulting large quantities of credit that became available generated a highly-leveraged economic climate, and pushed up asset prices to an unsustainable level. These asset prices eventually began to collapse, causing individuals and companies to default on debt obligations. The resulting panic among lenders led to a large withdrawal of credit from the crisis countries, causing a credit crunch and further bankruptcies. Investors attempted to

withdraw their money, the exchange market was flooded with the currencies of the crisis countries, putting depreciative pressure on their exchange rates. In order to prevent a collapse of the currency values, these countries' governments were forced to raise domestic interest rates to exceedingly high levels (to help diminish the flight of capital by making lending to that country relatively more attractive to investors) and to intervene in the exchange market, buying up any excess domestic currency at the fixed exchange rate with foreign reserves. Neither of these policy responses could be sustained for long. Very high interest rates, which can be extremely damaging to an economy that is relatively healthy, wreaked further havoc on economies in an already fragile state, while the central banks were hemorrhaging foreign reserves, of which they had finite amounts. When it became clear that the tide of capital fleeing these countries was not to be stopped, the authorities ceased defending their fixed exchange rates and allowed their currencies to float. The resulting depreciated value of those currencies meant that foreign currency-denominated liabilities grew substantially in domestic currency terms, causing more bankruptcies and further deepening the crisis. Many economists have downplayed the role of the real economy in the crisis compared to the financial markets due to the speed of the crisis. The rapidity with which the crisis happened has prompted many economists to compare it to a classic bank run prompted by a sudden risk shock. Other economist pointed to strict monetary and contractory fiscal policies implemented by the governments on the advice of the IMF in the wake of the crisis, while others point to the role of asymmetric information in the financial markets that led to a "herd mentality" among investors that magnified a relatively small risk in the real economy. The crisis had thus attracted interest from behavioral economists interested in market psychology. The role of the International Monetary Fund was so controversial during the crisis that many locals called the financial crisis the "IMF crisis. To begin with, many commentators in retrospect criticized the IMF for encouraging the developing economies of Asia down the path of "fast track capitalism", meaning liberalization of the financial sector (elimination of restrictions on capital flows); maintenance of high domestic interest rates in order to suck in portfolio investment and bank capital; and pegging of the national currency to the dollar to reassure foreign investors against currency risk. In other words the IMF itself was the cause.

Current 2008 financial crisis

This current crisis confronted both national financial system and international financial system. The beginning was with failures of large financial institutions in the United States, it rapidly evolved into a global crisis resulting in a number of European bank failures and

declines in various stock indexes, and large reductions in the market of stocks and commodities world wide. The crisis has led to de-leveraging
and liquidity problem. In the fall of 2008, the credit crunch, which had emerged a little more than a year before, ballooned into Wall Street's biggest crisis since the Great Depression. As hundreds of billions in mortgage-related investments went bad, mighty investment banks that once ruled high finance have crumbled or re-invented themselves as humdrum commercial banks. The largest American insurance company and the largest saving and loans company were seized by the government.
The channels of credit, the arteries of global financial have constricted cutting off crucial funds to consumers and business (small and large).

In response, the federal government (USA) adopted a $700 billion bailout plan which meant to reassure the markets and get credit flowing again. But the crisis began to spread to Europe and to emerging markets, with governments scrambling to prop up banks, broaden guarantees for deposits and agree on a coordinated response. The literature of the crisis gave several reasons of what trigger the crises some of it are:

1- The absence of regulation of Mortgage Company the adequacy of its capital was waived by the American regulators
2- The absence of regulation of sub- prime (high risk mortgage debit) Mortgage Company and this led to their indefinite leverage ratio.
3- The absence of regulation of the bond rating agencies which have rated the risky bonds according to the fees paid.
4- Unregulated institutions like hedge funds and private-equity firm which had the ability to take much bigger risks than regulated banks and unlimited leverage.
5- Commercial banks are regulate and protected as opposed to investment bank which have the freedom to speculate freely, most of the American do commercial banking, investment banking, stock brokerage and even insurance that is are becoming financial supermarkets.

These underlining reason demonstrate that the absence of regulation the relaxing application of the regulations and the finding of ways round the regulation are the core of the reasons for financial turmoil in the American financial system. This call for regulation and monitoring systems which help in early detection and timely recognition of financial vulnerability and the formulating and implementing the required corrective measures.The literature in general blame on regulatory failure to guard against excessive risk-taking in the financial system, especially in the U SA.

Countries through out the world are bailing out the financial systems in their countries because the financial system crisis is leading to an economic recession which will spill over to become a wide world recession. The international organization contributed to bail out some member countries but did not propose any solution to overcome the crisis. The response was only warning no practical solution was presented contrary to the response to the Asian crisis when there was a quick identification and response to the financial problems. Some economists think that may be the failure to over the Asian crisis and the recurrence of the other strong financial crisis made these organizations more reserved. On the other hand many Islamist economists presented a way out of this crisis by applying the Islamic economy rules and regulation. Many world leaders are calling to “recast the capitalist system” and to create an international system to watch over the world’s banks. Some economist said that this was a failure of the Capitalistic economic system and a review is necessary

Second part

The role of Financial International organization

At Britton Woods in 1944 and Savannah in 1946 the task of both the International monetary fund and World bank were outlined according to the to the financial circumstances of the 21st century. Later in 1976 the Second Amendment to the Fund Articles were made. In this presentation the focus is on the WB and IMF's task in promoting national and international financial stability as a part of their mandate in 1944 through financial surveillance, financial assistance and technical assistance. The WB and IMF have three important roles in international financial crises. The first is to help countries to fashion programs to rest on currency and market stability. The second role, under certain circumstances at least, become a lender of last resort. The third is as a rallier of others in support of actions necessary to end the crisis. Therefore the Fund's surveillance activities are the core task it focuses on the sources of crisis vulnerability and on strengthening crisis resilience. That is should be able to assist countries:

- To forestall crises
- To adapt programs and policies to rapidly evolving circumstances.
- To prevent crises from escalating

Surveillance is the backbone of crisis prevention. It must also be implemented by implementing stability-oriented policies and to be effective, surveillance periodically requires a reassessment from a fresh perspective that is fully cognizant of evolving economic and political circumstances especially in the last decades (see table 1and 2) which are characterized with financial instabilities and crisis the recent of which is under treatment. There are several programs launched to carry the task of Surveillance in response to the different countries financial turmoil that affected international financial systems. The three chosen important programs launched as a response are explained to illustrate the role of the IMF and WB in the task of surveillance are.

[i] The financial sector assessment program FSAP

The Financial sector assessment program is a joint IMF and WB initiative introduced in1999 as a response to the nineties' crisis. The aim of the program is to promote the soundness of the financial system by looking particularly at the structure and the regulation of the financial sector. The program is a tool for conducting systematic assessment of the country financial sector and benchmarking regulatory effort. The program is designed to identify the strength, risks and vulnerabilities of the financial sector. The program depicts four type of financial surveillance:

- Macro-prudential surveillance

- Financial soundness surveillance
- Surveillance of market financial condition to assess the risk of shock and analysis of micro-financial linkage
- Surveillance of macroeconomic conditions

The FSAP is designed to diagnose the potential vulnerability in both the national financial systems and the regulatory framework. To achieve this the FSAP uses a wide range of analytical tools and techniques that include:

- Macro-prudential analysis including stress testing, scenario analysis and analysis of financial soundness and macro-financial linkage
- Analysis of financial sector structure, efficiency, competitive-ness, concentration, liquidity and access.
- Assessment of observance and implementation of relevant international standards codes and good practice in the financial sectors
- Analysis of specific stability and development issues tailored to the individual country circumstances.

These tools and techniques assess the financial system through an assessment frame work and are based on first macro-prudential surveillance and financial stability analysis to monitor the impact of potential macroeconomic and institutional factors on the soundness and stability of financial system.

Second: financial system supervision and regulation to help manage the risk and vulnerabilities to protect market integrity and to provide incentives for good governance, transparency and anti-money-laundering. Third financial system infrastructure which consist of three types which are legal infra-structure, systemic liquidity infrastructure and transparency, governance and information infra-structure.

The first step in this program is to compile a set of different indicators the first set are the financial structure and development which comprise of system wide indicators, breath of the financial system, competition, concentration and efficiency of the financial system and scope and coverage of financial services. The second set of indicator are financial soundness indicator for the financial sector different components that is financial soundness indicator for banking, for insurance, for security markets and market based financial soundness. The third sets of indicators are aggregate balance sheet structure of financial and non financial sector linkage.

The second step is an overall framework assessment of

- Financial stability assessment which is referred to as Macro-prudential surveillance consist of financial sector soundness and its economic and institutional

determinants. It includes quantitative analysis of risks and vulnerabilities and qualitative assessment of the institutional capacity and financial infrastructure that help to manage the risks. It also complemented by information from qualitative assessment of effectiveness of financial sector supervision and of the robustness of the financial sector infrastructure.

- Financial structure and development assessment consist of assessing of the functioning of the financial sector including its scope, concentration, efficiency, competition, and adequacy of access and its institutional and economic determinants. The goal of this assessment is identify policy adaptations and structural changes in financial infrastructure.

An integrated analysis and assessment of stability and development can be summed up into assessing financial system (banking, insurance and security market) risk and vulnerability, assessing non financial sector condition, assessing the financial sector need sand assessing the legal institutional framework and operational effectiveness of financial policies.

<u>The third step</u> evaluate

1- Financial sector supervision of banking, insurance and security market this include

- Legal and institutional framework for financial supervision.
- aspects of financial safety net
- Assessing bank supervision specifically Basel I and II
- Assessing insurance supervision
- Assessing securities market regulation

2- Assessing the supervision of other financial intermediaries, rural and Microfinance institutions, financial system integrity (anti-money laundering and combating terrorism), information and governance infrastructure, legal infrastructure of the financial system and finally systematic liquidity infrastructure.

<u>The fourth step</u> this last step provide guidance on sequencing of financial reform which deals with factors that should be considered when setting priorities among a multitude of polices, institutional, and operational reforms that has been identified as a result in the participation in the FSAP. The appropriate sequencing and coordination of reform will help in financial development which helps in avoiding financial instability. The IMF has review the FSAP in March 2003 by an independent evaluation office and by IMF operation evaluation department to provide information on the development and on the update on the analytical tools of the program and include proposal to help different countries to strengthen their financial sectors, to minimize vulnerabilities and to contribute to the intermediation that support growth.

[2] Financial soundness indicators (FSI)

The development of the financial soundness is coordinated by the IMF with the support of the World bank, the Organization for Economic Co-operation and Development, Bank for International settlement, and the European central bank. Financial soundness indicators are statistical measures for monitoring the health and soundness of the financial sector and its corporate and household counterpart. Financial soundness is included through the activities in the context of the FSAP and the survey on the use, compilation and dissemination of macro-prudential indicators. A compilation guide on financial soundness indicator was produced by the IMF with the purpose to arrive at clear definition of the indicators and of the analytical tools to be used.

The definition, the interpretation and analysis were undertaken by the IMF. The data compiled by each country facilitate monitor the financial system and can be compared at globed level this is important in view of the magnitude and mobility of international capital flow and the risk of contagion of financial crises from one country to another. Finally a benchmark is developed for the level of Financial Soundness Indicators that would help to monitor and interpretate development of the financial system. FSI are calculated and disseminated for the purpose of supporting macro-prudential analysis. This is the assessment and surveillance of the strengths and vulnerabilities of financial systems, with the objective of enhancing financial stability and, in particular, limiting the likelihood of failure of the financial system.

The FSI are two set of indicators that are considered useful for the purpose of periodic monitoring and for compilation. The core set which include indicators for the banking sector and the encouraged set which include additional banking indicators as well as other institutions and markets that are relevant to assessing financial stability. They will give valuable information on financial stability for a large number of emerging and developing countries, in particular helping to identify potential financial stability risks at an early stage. They may give an indication of any potential financial stability issues. Financial Soundness Indicators will also assist and complement other surveillance work being undertaken by international bodies. The FSI consists of

a- **Core set** for deposit-taking institutions Capital adequacy Regulatory capital to risk-weighted assets, regulatory Tier I capital to risk-weighted assets, Asset quality Nonperforming loans to total gross loans, Nonperforming loans net of provisions to capital, Sectoral distribution of loans to total loans, Earnings and profitability Return on assets Return on equity, Interest margin to gross income Non-interest expenses to gross income. Liquidity Liquid assets to total assets (liquid asset ratio), Liquid assets to short-term liabilities and Sensitivity to market risk Net open position in

foreign exchange to capital

b- **Encouraged Set** for deposit-taking institutions: Capital to assets, Geographical distribution of loans to total loans, Gross asset position in financial derivatives to capital, Gross liability position in financial derivatives to capital, Trading income to total income, Personnel expenses to non-interest expenses, Spread between reference lending and deposit rates, Spread between highest and lowest inter-bank rate Customer deposits to total (non-inter-bank) loans, Foreign currency-denominated loans to total loans, Foreign currency-denominated liabilities to total liabilities, Net open position in equities to capital, Large exposures to capital Other financial corporations, Assets to total financial system assets to GDP Non-financial corporate sector, Total debt to equity, Return on equity Earnings to interest and principal expenses, Net foreign exchange exposure to equity Number of applications for protection from creditors, Market liquidity Average bid-ask spread in the securities market, Average daily turnover ratio in the securities market Households Real estate markets Household debt to GDP, Household debt service and principal payments to income Real estate prices, Residential real estate loans to total loans and Commercial real estate loans to total loans

[3] Assessment of compliance with Basel Core principle for effective banking supervision

IMF recommended assessing the observance of the Basel Core Principles conducted by the authorities of countries participating in FSAP. It should be prior to the FSAP or at the request of the FSAP team, and a questionnaires prepared by the staff of the IMF is filled out by the authorities of the country in preparation for the FSAP.

The assessment of observance of each of the Core Principles follows a

Qualitative approach and is based on the Core Principles Methodology (1999). The assessment method consisted of examining the degree of observance of each of a principle’s essential criteria and, where the assessor's judgments are based on the law applicable to the supervision of banks.

To assess the compliance a general macroeconomic background that is relevant to the financial sector is to be describe therefore a description of the structure of the financial markets and, in particular, the banking sector, the number of banks, total assets to GDP, basic assessment of the stability, capital adequacy, profitability and risk profile of the sector, and information on ownership, i.e., foreign versus domestic, state-owned versus privately-owned, and similar information. Furthermore, it should provide an overview of the supervisory environment (e.g., the mandate, role and functions of the local regulatory

authority, the role of self-regulatory organizations, oversight and regulatory arrangements, legal and institutional framework, transparency, public disclosure, and accountability practices). It should also summarize the capacity, competence, internal controls, integrity of operations, and operational autonomy of the supervisory function. Then a review of the preconditions for effective banking supervision, as described in the Basel Core Principles document such as soundness and sustainability of macroeconomic policies (those aspects that could affect the structure and performance of the banking industry); a well developed public infrastructure, effective market discipline; and mechanisms for providing an appropriate level of systemic protection (or public safety net) should be considered. The core principles to be considered are

Core Principle
1. Objectives, independence, powers, transparency, and cooperation
1.1 Responsibilities and objectives
1.2 Independence, accountability and transparency
1.3 Legal framework
1.4 Legal powers
1.5 Legal protection
1.6 Cooperation
2. Permissible activities
3. Licensing criteria
4. Transfer of significant ownership
5. Major acquisitions
6. Capital adequacy
7. Risk management process
8. Credit risk
9. Problem assets, provisions, and reserves
10. Large exposure limits
11. Exposure to related parties
12. Country and transfer risks
13. Market risks
14. Liquidity risk
15. Operational risk
16. Interest rate risk in the banking book
17. Internal control and audit
18. Abuse of financial services

19. Supervisory approach
20. Supervisory techniques
21. Supervisory reporting
22. Accounting and disclosure
23. Corrective and remedial powers of supervisors
24. Consolidated supervision
25. Home-host relationships

Critique of the Role

The Fund's surveillance activities should focus more on the sources of crisis vulnerability and on strengthening crisis resilience. There is concern about the Fund's ability in assisting countries to forestall crises or to adapt programs and policies to rapidly growing circumstances. It is broadly recognized that effective surveillance periodically requires a reassessment from a fresh perspective that is fully cognizant of evolving economic and political circumstances. Above all, crisis prevention has to be strengthened through more transparency. More progress towards greater transparency has to be achieved since the programs seem not to have achieved their objective.

The IMF is criticized for being too reluctant to assess corruption, tax evasion and other governance issues in its surveillance. Such an assessment by the IMF is naturally fraught with difficulties because it is likely to be viewed by governments as political interference.

More work could be done on setting up a voluntary debt resolution forum. It is necessary to decide the role the Fund should have in relation to such a Mechanism. The IMF would often be a creditor towards countries whose debt is being treated by a debt resolution forum. Because of this potential conflict of interest, the Fund's role in such a mechanism is not easy to define. Ideally the IMF should be able through its surveillance function to prevent crises from escalating. The proliferation of conditions in Fund programs has apparently been halted and awareness seems to be growing about the need to restrict the number of performance criteria and to ensure the achievement of its goal.

Lastly the IMF and WB exerts pressure on low income country more than high income countries which usually are the sources of financial turmoil to themselves and other countries in the world

Recommendations

IMF has to redefine its role in the global economy, the global financial crisis has created an opportunity for the IMF to reinvigorate itself and possibly play a constructive role in resolving, or at the least mitigating, the effects of the global downturn, on two fronts:

(1) Contributing to long-term systemic reform of the international financial system

(2) Through immediate crisis management,

Here are some recommendations to achieve this:

- The tasks of the IMF and world bank should be reviewed and should adapt programs and policies to rapidly evolving circumstances
- IMF should continue to concentrate its work on surveillance, financial assistance and technical assistance. The role of the Fund to member countries should be to address issues affecting macroeconomic development. Issues that can have macroeconomic importance .Fund therefore has to be able to address a wide range of problems with macroeconomic relevance.
- IMF with the cooperation of World bank should create a global bank regulator
- Improving Co-operation between the IMF and the W Bank has to be improved to avoid conflicting advice or severe duplication of effort between them.
- To accommodate more African chairs and to create better possibilities for increased representation of some Asian countries.
- The Role of the IMF in Low-Income Member Countries should be at the right balance between its core role of helping them to achieve macroeconomic and financial stability, and responsiveness to special problems such as clearing debit arrears and providing emergency help.
- IMF's existing instruments should be adequate for dealing with the challenges facing low-income countries in various stages of development.
- Development Goals by focusing on its core areas of competence by promoting a stable macroeconomic and institutional framework for private investment and growth for low-income members.
- The staff of IMF should put firmer emphasis in their surveillance to assess the implications of policies of the major economies for global economic growth and to encourage policy reforms in industrial countries,
- It is important for the IMF authorities to remain in close contact with development aid authorities and WB authorities to ensure consistency of the views expressed.
- Shareholders of the IMF, through the Executive Board, have the responsibility to take sensible decisions to safeguard the credibility and soundness of the institution.
- The IMF should be a forum in which countries can discuss financial risks. It should also hold countries to account. In these ways, it can indirectly support global monetary stability.
- The IMF must not only be competent and financially sound, it must also be able to preserve its own independent judgment outside international political pressure.