

NEW IDEAS IN DEVELOPMENT AFTER THE FINANCIAL CRISIS

KEYNOTE ADDRESS

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JESSICA EINHORN: Guess who came. (Laughter.) Good afternoon. I'm Jessica Einhorn, dean of SAIS, and I am delighted to be here to welcome you back. I have the honor of introducing Dominique Strauss-Kahn for a keynote in the SAIS-CGD Conference on New Ideas in Development.

We are coming to the end of our discussions, and at this stage we are all eager to look beyond the present crisis and think about a future world which will have learned good lessons and is ready to take up the mission again of pursuing peace and prosperity through multilateral cooperation. Who better to get us started on that journey than the managing director of the International Monetary Fund?

Monsieur Strauss-Kahn took up leadership in the IMF in November 2007. We know now that by that time we were at the doorstep of our recession in the United States, but no one could at that time mark that moment. Indeed, the challenges of the MD's first year would be in defining a relevance and an operating model for the IMF at a time when demand for resources had dwindled, shouts for governance reform filled the air and ambivalence on surveillance by key members challenged the institution.

But just as the LDC debt crisis in 1982 propelled the IMF and shocked the Jacques de La Rosière into global leadership, so has this crisis reminded us all of the need for our multilateral institutions, particularly when they are headed by a Frenchman, such as the IMF.

Member countries are fortunate to have found themselves at this time with an MD so superbly prepared to step into the center ring. Born in Paris with early years in Morocco, Monsieur Strauss-Kahn holds a Ph.D. in economics from the University of Paris. He also graduated in law, business administration, and political studies. So for our students here who are doing joint degrees, he's up-ed you one. (Laughter.)

It seems broad in scope, but he managed to excel in each field as he moved through his career. He began as a professor of economics, and maintained ties to the university life throughout his career, most recently as a professor at Sciences Po as it is known throughout the world.

In the 1980s, Monsieur Strauss-Kahn began his career of public service with election to the national assembly and his appointment to the economic planning agency. In the early 1990s, he served as ministry of industry and international trade, and then he practiced law in the private sector. In 1997, Prime Minister Jospin appointed him minister for economics, finance, and industry from where he led the socialist government's broad privatization program and became globally highly regarded for the strength of the French economy's performance during those years.

Having started out as a young member of the Union of Communist Students – (laughter) – he became celebrated – (laughter) – he became celebrated for his reforms as a socialist minister, preparing his country for the competitive challenges of an enlarging Europe and of course globalization.

Being of a similar age, perhaps a little older, I take the liberty to say that like so many who came to professional maturity in the '80s and rose to leadership in the '90s, he appreciated the opportunities that could come from the opening of markets and a lifting of the way-too-heavy hand of state administration. And of course he has lived to see that pendulum swing way beyond his initial tap into the center. But I remember well and personally from my perch at the World Bank in charge of finance how much inspiration he provided for those who saw the need for those international reforms. Indeed, it is at our peril that we would think of rolling back the clock in nostalgia for the state rather than repairing the partnership to move forward, or as I like to say, schadenfreude is for losers. (Laughter.)

Monsieur Strauss-Kahn is surely the right man to confront the enormous challenge of the present global recession and financial stress. In these busy days, we are enormously appreciative that the managing director has come to speak to us and I am pleased to welcome him to the podium.

(Applause.)

DOMINIQUE STRAUSS-KAHN: Well, thank you for those kind words. Good afternoon, all of you. It's a pleasure to be here, really, and have this opportunity to talk about multilateralism and a need for global cooperation and macroeconomic and financial sector policies.

We all know that decisions taken in isolation end up harming the global economy. That's a classic problem of coordination, and it becomes more glaring during time of economic distress. I think that one of the key lessons of the Great Depression were that the lack of cooperation makes things worse, dramatically worse, the unprecedented collapse of the global activity in the '30s also had dire social and political consequences. As everybody knows it contributed even if it was not the only reason for the outbreak of a disastrous war, what left millions dead and a whole continent in ruins.

So when world leaders met in Bretton Woods in 1944, they vowed never to repeat the error of the past, they embraced multilateralism and cooperative approach to economic and financial policy, and that was really what are the beginnings of the IMF. IMF was born, as you know, in this meeting in Bretton Woods, forged in the furnace of this multilateral idealism with a mandate to oversee the global financial system, to help members with the balance of payment, payments needs, and also to be in one way or another at the heart of this macro-financial – macroeconomic and financial sector policy coordination.

That is why I am very pleased to say a few words in the midst of the crisis with some good example and some less good example of coordination, and say a few words about multilateralism in general and the way it applies to the IMF.

Over 60 years later, although the contours of the world would be probably unrecognizable to the Bretton Woods delegates, the IMF remained in my view as central as ever. But it took the financial crisis since the Great Depression for this to be manifest. It's a bit of a surprise because as globalization and financial integration accelerated over the past decade or so,

it might seem obvious that the multilateral institution would be more useful, and in fact the reality was different. Over the last eight years, it appears more and more that those multilateral institutions were finally maybe not that useful.

Eighteen months ago when I joined the IMF, the institution was facing progressive loss of relevance and legitimacy. People were questioning the usefulness and the very nature or the future – the very future of the institution was at stake. So we went through much soul searching, we went through a painful downsizing, and now 18 months later, it's as if it was a lifetime now in the midst of an economic crisis, certainly originated in the U.S., in the housing market, but immediately – has immediately infected the advanced economies and spread like wildfire to have a corner of the world.

And as the dust settles, we have learned a few core lessons. We have been learning that the links between the real economy and the financial sector are deep rooted, and that the world economic interconnections are probably – between, among countries are probably more important than we had imagined before. We have learned that multilateral solutions are essential. We have also learned that the IMF is ideally placed to address this kind of financing and liquidity problems at the global level. So I'll try to address in turn the different points.

The first one is the traditional role of the IMF, the role as a firefighter. The crisis has shown that while a firefighter may seem useless when you're in quiet times, they have a major role when things turn sour. And as for real firefighters, there is no way to say because there's no fire that you don't need the firefighters, so this idea that because you were in quiet times, you don't need an institution likely to provide support to countries in case of crisis was probably a very wrong idea. It has been proved wrong very rapidly.

The IMF has been helping emerging countries cope with coping with the sudden stop in capital inflows on which they have been heavily relying on the last decade or so. The IMF has been also helping advanced economies. Take Iceland, for instance, a very rich country undone by leverage, and what about the low-income countries? There has been this debate, as you know, a debate in the last 10 years, whether or not should IMF be involved in low-income countries. Wasn't it a job for the World Bank and other development banks? Was the IMF focusing on emerging countries? In fact, I think it was, again, a wrong debate and that we have a lot to do in low-income countries. Those countries have been hit first time by the food and fuel crisis, and then by the collapse and trade and remittances.

And what is at stake in those countries, probably even more important – well, I won't say more important but as important in a different way – that what happens in emerging countries and advanced economies, the World Bank figures from this point of view are really scary. They say almost 50 million people could be pushed further into poverty this year. They say 3 million, 3 million additional children may die between now and 2015 if the crisis persists.

So what is at stake in this part of the world is that only – I say only – unemployment growing or losses in purchasing power. It's worth more than that; it's life and death. We could witness in those countries not only social unrest but also political instability, democracies are very young, and when democracies fold, you can also go into civil war or even foreign war. So

the situation in this part of the world – low-income countries are not only African countries, but are mostly African countries – the situation in this part of the world is as worrying for different reasons than the situation in other countries having more systemic effect, but not having a population in such a strong distress.

So the world community cannot let this happen, and that's why the G-20 in London three weeks ago have asked for an additional \$6 billion on concessional lending to be provided to this country, and we and IMF are really committed to achieving this goal. Because I see as you many people – and they're right in saying so because they have a political responsibility – arguing that things may go in a better direction. And it's right to say that there are some green lights showing that the – in some respects, the situation is improving.

But when you take the full picture, it's mixed. You have in fact two forces at work. The first one is pushing downward. It's the very bad last quarter of 2008, a real collapse in production and trade, and we're still having the consequences of this collapse – a Keynesian (ph) effect, the collapse in trade, then collapse in production and exporting countries, and there's a vicious circle which begins.

At the same time, we have some glimmers of hope, as somebody has said, coming from the fact – mostly from the fact that stimulus packages which have been implemented begin to produce some reserves. At the time being, certainly the forces pushing downwards are stronger than the forces pushing upwards, and that's why our forecast for 2009 we just released yesterday are still very, very worrying: minus 1.3 percent of negative growth, shrinking of the global economy is something terrible. It means figures around four, five, or six for the big emerging economies, India and China, but on the other hand, minus four, minus five, minus six from advanced economies.

So it's really scary, and in the same time, that's a bad sign, but at the same time, we still believe that the recovery is possible at the first semester of 2010 providing that the right policy are implemented. So I will come back to this problem of the right policy because it's really the main point which is today at stake. But what is sure – that even if the best policy I implemented 2009 will be a terrible year. And as the crisis evolved, the IMF is trying to do its job, mainly providing to the country having financing gap the necessary resources not to collapse.

So we need to beef up our firefighting arsenal, and that's what has been done at the G-20 in London with the tripling of our capacity – of lending capacity, and not only the tripling of our lending capacity to the emerging countries, which is the biggest amount, but also almost the tripling of our capacity in concessional lending to low-income countries.

At the same time, the problem for us is not only to have resources and to use it for the international community, but to have the new tools to do it because as the – with the world engulfed in the worst crisis in generation, there's no way to do business as usual, and old tools have to be reshaped and redefined to be able to face the problems of today.

For instance, I don't want to enter into much technicality, but we just doubled the access limits for the different countries, including the low-income countries, which means the country –

the problem for us is not only to have the resources likely to be provided to the countries, but also individually country by country to have possibility for them to borrow, because if we say we have a lot of resources, but you're not likely to borrow more than a couple of hundred of millions because your debts sustainability is not good enough, then what's the use of the resources. So we have to manage on one hand having enough resources, but on the other hand having the tools which make them effective.

At the same time, it's clear that it's better to prevent fires than to put them out. To prevent fire rather than put them out means to have some kind of insurance facility, which make it possible for countries to insure themselves, avoiding the building of huge currency reserves, which are part of the contribution to the global imbalances and the country relying on this insurance policy so that they know that if needed, they will find the resources.

But the IMF and no other multilateral institution in the same way, it never succeeded in the past to build this insurance facility. It just has been defined months ago, and we already see that this flexible credit line, which relies on the good track record from the country in the past, but not asking for strong conditionality for the future, no conditionality at all as a matter of fact – just asking the country to go on with the policy which they have already implemented because they have the right policy in place. This new facility already gained interest from Mexico, from Poland, from Colombia, and I am convinced that some others are lining up.

So it does not mean that for the IMF today conditionality is not important; conditionality is very important. For many countries, there is no way to provide them with the needed resources without at the same time correcting the policy in place. Very often, the problem will come from the fact that the policy in the countries had been, let's say, not as good as they should be, mostly on the fiscal side, so they are facing huge fiscal deficit, converted in huge current account deficit and that's why they come to the IMF so the IMF can provide resources to fix the current account problem. But if at the same time, you don't fix the fiscal problem which was at the root of the question, you just waste your money, and after one year or so, you're back to square.

So obviously conditionality, which means we give you money, but at the same time, you have to change your policy, remains something very important. But that's true for countries where we want the policies of change because we believe, right or wrong – I think mostly rightly – that policy in place are wrong. But the new thing in this process is that there's a lot of countries – a lot of countries having derived policy in place just being hit and hard-hit by the global slowdown, and especially emerging countries, having relied on the very large inflow of capital during the last decade, which is right for emerging countries, and just seeing this inflow of capital dried up because of capital repatriation by Western banks. And so they're facing huge financing gap that didn't do anything wrong; they have nothing to change in their policy just going on with this policy, but nevertheless, they need a huge amount just to bridge the gap.

So this idea that the new kind of conditionality has to be defined – sometimes very strong when really the policy has to be changed – sometimes very light when there's nothing really to change, and at the same time that this conditionality has to focus on the problem which is – which to be fixed.

You know, in the past it was often the case for IMF staff and management of course to have this will that they could fix the world. So they were dealing with the country and they wanted to fix all of the problem of the country, even those who have very little connection with the problem at stake. And of course fixing all of the problem in the country, even if you are right, makes a lot of political problems.

So part of the bad image of the IMF comes from the problem the institution had with some of its members just because they wanted – because they were cold for one specific problem to deal with older problem. Having more focused conditionality on what is really at stake is certainly something that we are doing now, and which is useful, and at the same time introducing some new kind of conditionality which I call social conditionality, which is to take some part of the available resources, even when they are very scarce, to help the most vulnerable part of the population, the poorest part of the population to cope with the adjustment – economic adjustment always is very painful – but even more for the poorest part of the population.

And one of the reasons why in the past this intervention of this multilateral institution, which is supposed to come to help the country was not seen as helping, is because this adjustment was very costly for this part of this – this most vulnerable part of the population.

So in Latvia, for something as big as one-and-a-half percent of GDP, in Pakistan for a little less – something about 0.5 percent of GDP, but 0.5 of Pakistan GDP is not small money – we really tried to build with the country some special plan directed to the most vulnerable to make this adjustment more acceptable for the population, not only for ethical reasons or, I don't know, any kind of socialist philosophy – no, no, no – just because the ownership of a program by a country is something which is a very important condition of its success. And if the country rejects the program, then it's very difficult to have a success.

So this ownership doesn't rely only on the fact that you will have the most vulnerable – but certainly part of it, and I think that this social conditionality that we implement everywhere, including in low-income countries, where we have explicit target and – (inaudible) – and education spending, I'm sure that this changes the face of this institution.

I spent a lot of time on this because in my view, multilateralism, as you may understand, is absolutely essential, going to be even more essential in the future but it has to be accepted. If it's seen, we have to be seen as doctors by our members, not as cops. In the second situation, they will reject the fact that we want to help them, and the effectiveness of our job will be destroyed.

Effectiveness is certainly a question of financing. It's also a question when we deal with – when we write to be a policy advisor. That is a very big function for a multilateral institution. When a country gives advice to another country, it's never well-received. I won't say that when a multilateral institution gives advice, it's well-received, but at least it's multilateral, so it's a bit easier to accept.

And I really think that the IMF was the first to pinpoint the policy responses to this crisis, which is now part of conventional wisdom, and not least in two key areas. The first is the fiscal stimulus and the second is the need to restructure the financial sector. Let me begin with the fiscal stimulus.

As you all know, or should know, it's as early as January 2008 that the IMF has asked for a global stimulus in countries having some room to do it. At the beginning it has been received a bit – with some surprise – it was kind of a novelty for a country which is better known for belt-tightening than for asking for fiscal ease. But we said that because we saw already at the beginning of 2008 that the decline in demand will be exceptionally large, and at the same time, that military policy will reach rather soon its own limits, and so something else has to be done.

And argue at this time that it was not possible to have this fiscal expansion everywhere. Some countries don't have fiscal room to do it, but everywhere it was possible, it has to be done, and moreover, that this has to be done in the coordinated way to be more effective. Today in 2009, the 2 percent of fiscal stimulus which has been asked by the IMF has been delivered by the country. We're exactly at 2 percent, which is fine for 2009. We will see where we are for 2010, but so far, for 2009, the effort which has been provided by the different countries is in line with what we ask.

And really, I must tell you, I have been impressed by the unprecedented international coordination which took place, contrary to what is often said. I often heard some complaints saying there's not enough international coordination, which in general is true. But on this question, the international coordination has been big enough so that for the first time in history, all of the countries having some fiscal room go in the same direction at the same time, providing the same kind of policy for only a request of a multilateral institution so that at the end, the recession is still there. But our estimate is that thanks to the fiscal stimulus, we probably are 1.5 to 2 percent of gross higher than we will be if we hadn't faced a fiscal stimulus.

I could say the same thing – or not exactly the same thing – on the need for the clearing (ph) of the balance sheet of the banking sector. The same thing – not the same thing – the same thing is that since March, April 2008, one year ago, we started producing paper to the different governments, including the U.S. government saying that we have experience of a banking crisis. One of the experience of the IMF is to have dealt with 122 banking crisis – some very small, some big, over the last 60 years.

There are very different countries, different time, different structure of their industry, but sometimes you have some constant. And one of the few constants which we see everywhere is that you never recover before you cleaned up the balance sheet of the financial sector. You can postpone it, you can wait, but if you wait, you postpone the same way to recovery.

Everybody has in mind a very well-known example in Japan where in the Japan crisis, the authorities put in the economy huge amount of money, huge amount of stimulus without any kind of result, and dealt – they accept this idea that they need to cope with the financial sector. So that's the same way that the fiscal thing – I think that today everybody, almost everybody agrees that that's the right policy to implement.

And I was very much impressed at the meeting of the head of state in governments in London that most of them were well-briefed and acknowledging the fact that, yes, we know that that's what we need to do, we understand that the fiscal is fine, that's done. We'll see for 2010, but what we need to do today is really to clean up our financial sector.

The problem – and that's the difference with the stimulus, that when they come back home, they still believe the same thing, but they don't always deliver. And the problem is that it's very difficult politically. You know, when you go to your parliament or you're facing your taxpayers, voters, saying, yeah, we're going to have a deficit for a fiscal stimulus, and we're going to build bridges and schools and hospitals, you may have some people saying, okay, but that will be debt – will be a problem – fine, but nevertheless you have the support because people feel that's positive.

When you go to see the same guys saying we're going to put a lot of money in the banking sector when everybody rightly have in mind that all of this mess come from the banking sector, it's very difficult to get through. And so I understand that political difficulty for most governments to obtain from their government the support for doing so, and the people – and that's probably the reason why they're so reluctant. On top of that, some don't have money anymore. Some others have some ideological limitations – well, but taken around, the problem is that – I won't say nothing is done for this cleansing of the financial sector, but it doesn't go fast enough obviously.

And that's what I had in mind previously when I told you that the recovery can come in 2010 providing the right policy one implemented. There's two policy. One is a fiscal, fine. The second one is this cleansing of the financial sector, and it will be unfair to say that nothing has been done; that's wrong. But clearly it has to speed up, and if it doesn't, then the possibility of having this recovery in the first half of 2010 will be gone.

So I'm very worried today about the fact that the things are moving, but it's not moving quick enough – including in this country where the plan which has been released by the authorities – I think very well-shaped and adapted to the situation, but relies a lot on the willingness of the private sector to cooperate with the public side, and if they don't, nothing will happen.

So still we don't know. Will it work or not? It's not that obvious. There's a lot of techniques to deal with the financial sector. I'm not going to – don't be afraid – to elaborate too much on this, and all have advantages and drawbacks, and we can argue for hours you should do that, you should do that. It's not time to argue anymore; it's time to do it, whatever the problems that this technique or this other technique may have.

And I see a lot of debate in my own country or Europe, even here on the radio, sometimes on the TV with specialists and experts, academics, bankers arguing that you should do this, you should do that, but we're arguing a lot; we're not doing it. And really what's going to happen in the world global economy in the coming six months, and after the consequences in 2010, in 2011

relies a lot today on the – our capacity to be bold and really transform the situation of this financial sector.

So some good news, some bad news: The good news is that fiscal policy begins to deliver. The bad news is that it won't be enough and it won't be effective if the freeze of the credit flows is not addressed and if this credit flows do not resume as soon as possible.

Let me address in a few words – I promise to be short – another problem. I talk about effectiveness of the multilateral institution, especially the fund as a firefighter, as a policy advisor. But again, effectiveness is not the only part of the story. There's another part of the story which is the legitimacy of those multilateral institutions.

Let's look at the first kind of legitimacy, which is the legitimacy in providing early warnings. I've been talking a lot about the multilateral institution evolving during the crisis, but what about predicting the crisis. Multilateral institution, the World Bank, and especially the fund have been accused of sleeping at the wheel. And I have to say I take some of this criticism. It's fair to say that most of us, including the IMF made some mistake. It's fair to say that in 2005, 2006, 2007 probably those institutions gave warnings but not loud and not clear enough.

They – we – let's talk about making some criticism so let's talk about the IMF rather than other institutions. We have been too optimistic about the economic situation in the advanced economy. We fail to pay enough attention to factors like excess leverage, a system at risk, credit booms, asset prices. At the same time, we did give some warning, but they often have been ignored by policy-makers because they were not vocal enough. You know, people don't like listening to Cassandra, and when the sky is almost blue and you come to see a minister and tell him, listen, the sky is rather blue but in one year from now it's going to rain, he's a fine guy; he says, thank you very much. If it's not such a fine guy, he says something a bit – and in between, he probably has some election or something like that – say, okay, come back in one year; we'll talk about this one year.

So nobody wants to listen so much to early warning. Everybody on a rational basis is asking for early warning. And in the G-20 communiqué from London, you have a big paragraph asking the IMF to provide candid, even handed the early warnings – fine. But we will try to do it – well, we're still doing it, and we will at the spring meetings give a dry run of a new set of early warning with a new methodology which I think is very interesting. The problem is that that's a dry run, so it's okay, but when we will come to the real stuff at the next meeting in Istanbul, I'm not quite sure people will be so happy to have this kind of early warnings. On the other hand, it's ridiculous to break the thermometer and not to be able to measure the fever.

So because we have proved our worst once the crisis broke by giving one year ago, exactly one year ago at this pre-meeting in 2008 a set of forecast, which has been seen at this time as over-pessimistic, and we have been a lot criticized at this time for this reason, but finally it had been true. And in September, October, everybody came back saying, well, you were right. So we gained some credibility. That's probably the reason why now a lot of our members are asking this new kind of exercise.

But this legitimacy relies on the accuracy of what we say, and it's true for forecast; it's true also for what we say about the total losses in the banking sector, which has been released yesterday or the day before yesterday and the global stability financial report. Looking ahead, we intend to do better early warnings, but in this case we must not try from naming and shaming. I find there is no use for this. And so I'm afraid that IMF, while today it has a lot of friends, will not have so many friends later. But that's our job. And I think we have no reason to try to escape.

Before I conclude this afternoon, let me address another topic of legitimacy. Because legitimacy is very important, because it's the – for a global institution it's the tie that binds everything together, with no legitimacy or not enough legitimacy, a country will not approach us until it's too late. They will try to avoid coming to us because they don't like the institution. With no legitimacy, the mere existence of the flexible credit liner I was describing a few minutes ago will not prevent – (inaudible) – instruments from the country because they will not rely on this instrument and then they will build their own reserves contributing to global imbalances.

With no legitimacy nobody will listen to our policy advice. With no legitimacy, nobody will take our early warning seriously. So the legitimacy of the institution is part of its effectiveness. And to increase, to improve our legitimacy, we clearly need not only an old and multilateral institution, but it started with the IMF to reform our governance structure, to give more influence to emerging countries, to low-income country, and to rebalance the balance of power and the institution in a different way than what we have today.

The reform process has started one year ago. It's a dynamic process which tried to have different step and have different round of restoring legitimacy. What has been decided at the G-20 is to speed up the process and not wait five years, as was previously expected – 2008 – the next step was supposed to take place in 2013. So the G-20 asked for something in 2011 – speeding up the process. And I'm very happy about that even if it's not easy to do.

But what some of you or most of you, having looked at this question of quota and voice and representation in the IMF let's have in mind that legitimacy is not only a question of quota and voice and representation; it goes much beyond this. We also need for better legitimacy to do a better job in reaching out to civil society. The question is not only our membership. Our legitimacy relies also on CSOs that are interested in what's going on in multilateral institution.

I could say also that our legitimacy doesn't rely only on the share of the member – only on the share and the quotas of the membership, but for instance of the structure and a diversity in the staff. How can you really deal with the problem in a country with a specific culture – in Asia and Africa – in Central Asia and Latin America if everybody in the IMF or in the World Bank – which is less the case in the World Bank than the IMF; they are much more diverse than we are, but let's talk about the IMF. If everybody has the same training, the same culture, come from the same university and finally has no real experience of the grounds, all of the history, the political situation in the country.

So it's not only a question of increasing the quota from this country from 1.7 to 1.8; it's even as much having a real multilateral institution, which mean an institution likely to put

together different culture, different training, different spheres. That's difficult to do, but that's absolutely necessary because again the legitimacy of the institution is part of its effectiveness.

So let me briefly conclude. I have argued that robust multilateralism is essential, not only in the resolution of the current crisis but also in the prevention of future crisis. I have argued that we need stronger global coordination in macroeconomic, in financial sector, on all of the fields where we give some political – some policy advice. As the crisis unfolded, we saw the benefits of cooperation in the way the central banks cooperates from the – (inaudible) – the Fed, the ACB, the Bank of England, Bank of Switzerland, and also we saw the benefit of the cooperation in the fiscal stimulus as I said before.

But we saw for the cost of none cooperation. For instance, with the temptation that to protect domestic market with different kind of protectionism including banking protectionism, which is a new kind of protectionism – when Western country's banks repatriate capital because they have a problem at home, they are creating a problem outside while solving the problem domestically. But there is no domestic solution to a global crisis. So we always have to balance the advantages for the global community of solving a problem in one place, creating another problem in another place. And that's a new kind of – (inaudible).

I have in mind the name of some finance ministers – saying finance ministers, everybody understands it's not the secretary of the Treasury – in a country where a rather big amount of money had just been voted by the parliament to rescue the banking sector, convening all of the bankers in its office and saying, okay, fine; now you get the money, but this money stay at home. You're not going to use it to finance outside. And this – it's understandable; that's human nature, and that's politics. But at the end of the day, that's harming the global economy more than it has. So we absolutely need to have more coordination including avoiding or fighting this temptation of protectionism.

I have also argued, and you're not surprised about that, that IMF has perfectly poised to play a critical role in this international financial architecture. Maybe some of you have seen one or two weeks ago – Time Magazine has dubbed it IMF 2.0. I like that. (Laughter.) Of course, we already did some things and we still have a lot to do. And because we still have a lot to do, I would prefer to discuss about IMF 3.0, which is still to build – better that we are working hard to complete – because it's not only – it's not enough to say that multilateralism is useful, that we know that the problem was no multilateralism, that we can make a long list of the advantages of a coordination or this kind of thing. And at the same time, the institutions or the institution which is in charge of that doesn't adapt and be able to deliver.

So I want to argue in favor of a multilateral response to global crisis, but I want at the same time to provide the two, namely the institution in line with this advice. Remember that at the end of the day, it's not about the IMF or the multilateral institution. All of this is about the global economy and the welfare of nearly 7 billion people who share this planet. And at the end of the day, the role we play today in this crisis will have a lot of consequences on the welfare of a million of people in the coming decades.

So your advice are welcome, and your participation in any of the different group we are trying to organize to deal with academics with the civil society organization with different kind of partners that we didn't use to meet so often, all of those efforts in my view are very important because certainly people working inside the IMF – the staff of IMF and members, finance ministers, Central Bank governors are very aware of the problem and they have very good ideas. But they have good ideas from inside, and we also need good ideas from outside, and that's why I'm so happy to have this afternoon with you. Thank you.

(Applause.)

MS. EINHORN: I'm delighted that – actually 3.0 is probably about social networking, so we're in the right place. But in any event, the managing director has agreed to take question to the extent that his time allows, and that's probably quite short. But may ask you when you raise your hand to also stand up, give us your name. Choose one question, because if you do two, he'll have to choose amongst them, and we'll move as quickly as we can. Thank you. Questions. Yes, please.

Q: I'm Nora Lustig from George Washington University and also CDG visiting fellow there.

You spoke about coordination and cooperation. And I think one area where it's also needed is among the multilaterals themselves because I think that some of the competitor advantage of the fund is different from the one that the MDBs have. And I think it would be very helpful to bring this together, particularly with your new view, which I'm delighted to hear that there is going to be some social conditionality or that there is already – (inaudible) – some of the multilateral development banks have already developed a lot of expertise on how to do that – do that well. So I was wondering whether that's on the table.

MR. STRAUSS-KAHN: Well, you're absolutely right. I do believe that cooperation among the multilateral institutions are not that bad, have been worse. You know, there was a mantra that the IMF and World Bank, while being at the – to a different side of the same street couldn't work together. The good thing is that Bob Zoellick, the current president of the World Bank, and myself, who did arrive in office almost at the same time so we didn't have bad memories, so we could start – (laughter) – we could start on a new footing. And in my view, and I think I can speak on his behalf, our relations are very good.

Nevertheless, first, IMF and World Bank is not all the world. There is other multilateral institution. And even if the relationship are good, it doesn't mean that there's no overlap and that we are not sometimes doing the same thing in a different way, which is not effective.

So we're working hard to try to have this coordination among us also. Inevitably there is some overlap. We're dealing ahead of the curve. We're trying to create an economic environment which is good enough so that the development agency – (inaudible) – World Bank are also MDBs are likely to come and finance projects. So we are at the starting point, try to create the good environment, and then the development agency came and financed for a long-term project and has – or in the different kind of development.

But there is some kind, some place where we overlap, and we need to try to make it more effective. It's more difficult with other MDBs. Just because the relationships are good, but they're not just across the street.

Nevertheless, I think that if we're talking about the development banks, it goes not badly, and probably the crisis has helped everybody to just forget old problems that may have happened between the institution to just look forward and try to work together. What is even more important maybe is to work – not more important – as important – is to work with other institutions which are not – (inaudible) – insured institutions – WTO obviously, and sometimes the ILO.

I was just in Geneva at the general assembly of the ILO one month ago because how can we have an institution working on labor economics having a knowledge we don't have, and that uses knowledge when we're defining or whole program. So I'm not saying that the ILO will come and do our job, but to listen to what they say, have better connection with them is certainly something which is useful. So even – not only the MDBs, but beyond the MDBs this kind of cooperation is absolutely necessary.

MS. EINHORN: Nancy Birdsall.

NANCY BIRDSALL: Well, that was great –

MS. EINHORN: Here comes the mike.

MS. BIRDSALL: Thank you very much, Mr. Strauss-Kahn. I think this speech here will mark up a moment of really opening up of the IMF. And many of your remarks will be well-remembered: the social conditionality, the naming and shaming emphasis. I did find, however, what you said about legitimacy and governance issues to just touch on the tip of the iceberg.

And I think there are many of us here in Washington concerned about how to ensure that the U.S. Congress welcomes the changes that are proposed to it, that will be proposed to it by the executive branch. We're concerned that it will be complicated, that the fear of Congress has chilled already what will go to Congress, and that this is mixed up with the general problem of the legitimacy of the IMF because of the role of the U.S.

So I wanted to ask if you wanted to comment – not to make it awkward for you; maybe it's a bad time to do it – on how do you see the problem of the veto, the effective veto that the U.S. has in the light of the recommendation of the Trevor-Manuel Committee to deal with that veto. And is there anything else about legitimacy. You raised double majorities before you went to the IMF. There is the issue of the success – your successor – may it be many, many years hence. But there might be a time.

MR. STRAUSS-KAHN: Maybe I won't ever have a successor. I will stay forever.

(Laughter.)

MS. BIRDSALL: I guess I'm just inviting you to elaborate a little more on the governance issues, some of which came up in the preceding session at this conference.

MR. STRAUSS-KAHN: Thank you for this question. I had more to see, but I see my watch and as I was so long that I shortened what I had said then on legitimacy and governance. That's a very important question; you were right.

You raised three questions, the question of voting, veto power, the question of double majority, the question of the selecting process for the managing director who could say the same thing for the World Bank. Veto: As everybody knows, the United States has a veto de facto because – not all, but many and the most important decision have to be made with an 85-percent majority, and the U.S. have almost 17 percent of the voting power so they can block.

It's fair to say that they're not the only one who can block. Any coalition of 15 percent can block. So the United States is the only country having alone this voting power. But any group of three countries, four countries, having 15 percent all together – the Europeans for instance – can block the same way. So to be fair, not only the United States is likely to have this veto. But is it good, the situation? I'm not sure. I'm not sure because it makes some decision very difficult to me. There's a lot of political papers reports, thesis, Ph.D. dissertation on should the 50-percent majority in a democratic society be the only way to make decisions. I'm not going to elaborate on this, but obviously 85 is a lot.

So the Trevor Manual report that you rightly quoted proposed for the decreased level to the 70 percent. You know, we already have 50 percent, 70 percent, or 85 percent majority depending on the question. So we could get rid of the 80 percent and put the 85 percent at the 50 – at the 70-percent level. Fine. I have no problem with that. It makes life easier for the managing director because it's easy to find the majority to step forward.

I'm not quite sure that the U.S. Congress is willing to do – would be willing to do something like this, but there are also other proposals. For instance, some have this idea to say it shouldn't be 85 percent of the voting power but 85 percent of votes cast. In these cases, if the U.S. or the European as a block are abstaining, that don't make it impossible to have a majority because you need 85 percent of those who votes or things like this.

So again, it becomes a bit technical or a bit boring, but the idea is that the – (inaudible) – more democratic institution, we needed a way or another to make decisions made by a large majority – maybe not only a 50 percent majority – a bigger – a larger than 50 percent majority but nevertheless not an impossible majority to make this decision possible. If not, you know, Brazil has today a quota share of 1.7. If after huge efforts this jumped to 1.9, what's the use of it if you need 85-percent majority and you can never have it? So this problem is certainly a problem to address.

The second problem you were quoting is double majority. Yes, I have been talking about double majority, and I think this is very important – majority of voting power, but also majority of either countries – one country, one vote – or chairs around the table after board. And I must

say that my own practice for the last 18 months is that no decision has been made without having of course the required majority in the voting power, but also the majority of the chair in favor of this decision just in an informal way.

So we could have this more formal. And that's the link with your third question, which is the designation or the election of the managing director. I think that's critically the right decision to start with where a majority of country could be useful. We could imagine a system where I have heard this proposal said by several people where to elect – to choose the, if any, my successor and also the same thing in the World Bank, for instance, it won't be enough to have a majority of the votes but also a majority of the 185 countries having at least one half of this number in favor of the candidate.

There's a lot of possibility. I mean, you know, imagination is very rich and we can imagine lots of solutions. The problem is not that much to find the right solution – everybody has his own idea – the problem is the willingness to do something. And I do believe that we are in a period where it's a bit surprising. We could say with a crisis and in a crisis we only deal with the crisis, and we are not going to deal with other questions; we will postpone this question of governance later. But that's not the case. And many people, including among the members and the ministers and the head of state and government, are convinced that part of the problem comes from failure in governance, and that the question of improving the governance has to be addressed at the same time as we're fixing the crisis.

So I think it's the right time to move – again, I have given some examples as I have read in different review or listened from different committees. There's a lot of ideas on the table, but that's the time to discuss them. And my proposal would be that we try to make some progress for the next big meetings of the IMF which will take place at the beginning of October in Istanbul, which gives us six months.

And in six months, I'm sure that many of those ideas could be looked at, those things. This has – this has – this kind of – (inaudible) – this kind of has advantages; this other one has – because it's always, you know, technical – tell it always in details. So good ideas when they're just saying a few words that's fine. When you try to implement it, you see that it's not always that easy, so we need some work on that. But I'm prepared to work with you, with all of the different stakeholders to try to make progress on this.

MS. : This will be the last question. Unfortunately we're running out of time.

MS. EINHORN: Last question. Let me take a – (inaudible, off mike).

Q: Thank you. My name is Adama Gae (ph). I'm from Senegal. I'm a fellow here at SAIS. You mentioned social conditions. Don't you have the feeling somebody may say these are public relations conditions in a way because in the past, your institutions have been accused, criticized for the shortcomings of its policies, especially in countries like those of us like in Africa.

So my question is by creating these social conditions that would raise the profiled image of your institutions, are we not dodging the real political conditions that in the past are used to implement and that are still necessary in order to address the shortcomings of developments in many places in the world, and in places like Africa where I believe there is the political bubble with poor leadership and this could be hardships on the way to development. Are you not putting in place the social conditions to avoid the hard questions?

MR. STRAUSS-KAHN: I know millions of people who are going to benefit from this social condition who will – probably will not be of your opinion. Sitting in Washington, it's easy to discuss about the usefulness or not of those social condition. But when you're far away in the country in Pakistan, where we, as the World Bank who organize the distribution of cash payments. When you – a poor pensionnaire, at the very end of the income distribution in hungry, and the government has decided to reduce pension, and we say you're going to reduce pension but not for this tale of people having low resources, I'm sure these guys I'm interested in our social condition.

I'm not saying it's fixing all of the problems. I'm not saying that this institution has had a goal to fight against poverty, which was not true. We have to take into account this question. It's not our mandate. But our mandate of providing financial stability cannot in my view be successfully implemented if we don't take it.

So it's not all PR social condition. It's not even trying to improve the image of the IMF. Who cares about the image of the IMF? (Laughter.) It's trying to help the people – hundreds of thousands, sometimes millions of people – to be able to survive for one year, two years, three years, in an environment where it's going to be difficult because when you have to adjust your economy, it's always difficult, but it's not difficult of the richest. The richest are sometimes a bit less rich, but it's okay to be just a little bit less rich. But the poorest, they're sometimes just at the level of subsistence.

And what we want to do, and what we're doing is to make it possible for those part – this part of the population just to not be the innocent victims of an adjustment which is generally due either to global contraction, and they're not responsible for that, or to bad policy implemented by the government, and they're not responsible for that, or even by some kind of corruption or bad government in their country, and they're not responsible for that also.

So it's a very traditional discussion. There's more to do. So if you don't do more, should you do a little? Yes, my answer is always yes. When you do one step forward, even if what you had to do is 10 steps forward, it's better to do it than stay without moving. So we do one step forward. We're going to try to do another step forward, and maybe over time we will reach the level that you are asking for. But the best way to get at the end of the process you wanted to organize is to start moving, and that's what we're doing now.

(Applause.)

MS. EINHORN: I can say that we now know what we mean by a keynote address. And I want to thank the managing director, not only for his remarks here today but for the window

he's given us into how well that organization is going to be led. Thank you very much. And may I ask us all to come back at 2:45. Bye-bye.

(Applause.)

(END)