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Statement by Mr. Hans Eichel
Minister of Finance, Germany
On behalf of Germany

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Minister of Finance of the Federal Republic of Germany
to the International Monetary and Financial Committee
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I. Global economy and financial markets

Global economy – Conditions for robust, non-inflationary growth remain in place, but risks are tilted towards the downside. Here, we would emphasize the possibility of persistently high and volatile oil prices and a disorderly adjustment of global economic imbalances. Although a gradual tightening of the still exceptionally benign financial market conditions seems more likely, aggregate shocks or rising inflation expectations could lead to abrupt adjustments. The broadly favorable macroeconomic environment should generally be used to improve fiscal balances and to strengthen fiscal sustainability. Structural reforms should be continued in order to increase resilience to shocks and to raise longer-term growth. We reiterate our view that global imbalances need to be reduced in a cooperative manner. We reaffirm our commitment to contribute to a substantial reduction of trade barriers to bring the Doha Round to a successful conclusion.

Germany – External competitiveness is strong and export demand remains supportive. Furthermore, conditions are in place for the recovery to broaden since the reforms of the social security system and the labor market contribute to an improvement of domestic demand and employment. We are confident that, despite higher oil prices, this will improve growth prospects. We remain committed to further structural reform and to fiscal consolidation.

Emerging market economies – The rapid growth and further improved resilience to shocks in many emerging market economies is welcome, although many weaknesses persist. We welcome the decision by China and some other Asian countries to allow more flexibility in their exchange rates, thereby contributing to an orderly unwinding of global economic imbalances. China should make use of this new flexibility. We welcome the further improvement in fiscal positions and debt structures in many Latin American countries. We encourage these countries to continue with prudent fiscal policies and broad-based structural reforms, particularly to improve the conditions for foreign direct investment.

Oil markets and energy policy – Against the backdrop of low extractive capacities, bottlenecks in oil processing, strong demand growth and insufficient investment, oil prices are likely to remain higher than expected in the foreseeable future. This is likely to spur investment in energy infrastructure, energy-efficient technologies, and alternative sources of energy, while also encouraging energy-saving behavior.

Additionally, obstacles to investment in extraction and refinery capacity should be removed and incentives for energy conservation should be improved. Countries wishing to mitigate the impact of higher oil prices on the poor should adopt measures that do not distort price signals. Oil market data should be provided more timely and comprehensively in order to enhance transparency and reduce market uncertainty.

II. Medium-term strategy, surveillance, crisis prevention, and crisis resolution

Medium-term strategy – The Fund's primary purpose continues to be promoting monetary and financial stability, thereby contributing to sustained economic growth. This objective should guide the current considerations on the Fund's medium-term strategic directions. We broadly agree with the key tasks which the Managing Director has outlined in his report to the IMFC. We consider surveillance and policy advice as the Fund's primary instruments, supplemented by well-targeted technical assistance. The Fund should continue to advise and support its members in strengthening their economic resilience and in becoming more attractive for stable private capital inflows. This should increasingly allow members to overcome times of economic stress without Fund financial assistance. For the Fund, it is now important to fully implement the reforms already agreed upon. We would like the Fund to remain an efficient and effective institution concentrating on its core mandate.

Surveillance should become more focused and selective, with emphasis on macroeconomic and financial stability, fiscal and debt sustainability, and international interdependence. In analyzing globalization, the Fund should concentrate on these issues. The Fund should pay special attention to exchange rate regimes and developments and their impact on global financial stability. At the same time, streamlining assessments of structural policies and completing the series of special reports on financial sector stability as well as on standards and codes remains important. Bilateral surveillance should as a standard procedure assess to what extent members follow the Fund's advice.

Access limits - Official sector financing needs to be limited in order to provide incentives for adjustment policies in borrowing countries, for prudent risk-taking by private creditors, and for safeguarding the Fund's credibility. Hence, regular access limits and the exceptional access framework should be applied predictably and consistently. This would ensure that Fund financing together with adjustment policies will contribute to restoring market confidence, while at the same time avoiding over-lending and prolonged use. Also, financial assistance should be carefully considered in view of a country's overall capacity to repay. We reiterate our firm belief that precautionary exceptional access to Fund resources is not compatible with the Fund's systemic role as a provider of emergency assistance at "not-risk-adjusted" terms. Precautionary exceptional access would also weaken private sector involvement and exacerbate moral hazard.

Financial position of the Fund – We welcome the further improvement of the Fund's financial position. The Fund should continue to reduce its current large exposure to a few members, and these members need to further lower the Fund's share in their total external debt. In addition to adhering to access limits, it will be important to apply a rigorous debt sustainability analysis in lending decisions and strengthen price incentives for early repayments in order to protect the Fund's financial integrity. An accelerated accumulation of precautionary balances should be considered. We welcome efforts to strengthen the Fund's income position such as creating an investment account.

Crisis resolution – Germany welcomes the rising support for the "Principles for Stable Capital Flows and Fair Debt Restructuring in Emerging Markets" that private sector organizations and emerging market countries have agreed upon. These guidelines encourage a cooperative approach to crisis prevention and resolution and can thereby make inevitable debt restructurings more predictable. The Fund should lend support to these principles and monitor their implementation. The implementation of the lending-into-arrears policy, including the good faith criterion, has proven to be difficult and should be reflected upon. We continue to urge Argentina to develop a strategy dealing with the claims of those private creditors that did not participate in the debt exchange, and to start to negotiate with the Paris Club on its outstanding obligations.

III. Development Finance and Multilateral Debt Relief

Millennium Development Goals (MDG) **–** The Millennium Development Declaration remains the framework for our cooperative efforts. More efforts are needed to achieve progress towards the MDGs, particularly in developing countries themselves, supported by more official development assistance (ODA). At the New York Millennium Review Summit, the EU presented a comprehensive package of measures. Part of this package is Germany's commitment to undertake to reach an increase of its ODA to 0.51 percent of gross national income in 2010 and to the target of 0.7 percent in 2015 that the EU has collectively pledged. Given the currently very difficult budgetary situation and obligations under the Stability and Growth Pact, Germany has made it clear that these ODA targets will only be achievable with substantial contributions from innovative financing mechanisms. To better cope with rising aid, the Fund, in close cooperation with the World Bank, should intensify its advice to recipient countries on public expenditure management, domestic resource mobilization, increasing absorptive capacity, and on how to respond to real exchange rate effects.

Multilateral Debt Relief – The G-8 Debt Cancellation Proposal provides a unique opportunity to complete the process of debt relief for heavily indebted poor countries (HIPC). We hope that the entire membership of the IDA, the African Development Fund and the IMF will seize this opportunity. Countries benefiting from debt relief need to adopt or maintain sound policies, improve governance and strengthen the environment for investment. Debt relief for post-completion point HIPCs should be additional, fully financed through a fair burden-sharing and subject to HIPC criteria and conditionality. In the process, the financial position of the International Financial Institutions must not be weakened. The HIPC initiative and the Debt Sustainability Framework should not be undermined. Although the Fund's debt relief should be financed primarily by its own resources, Germany and the other G-8 countries stand ready to provide bilateral contributions as necessary. Furthermore, Germany is committed, on a fair burden sharing basis and according to established criteria, to contribute to the costs caused by countries that may enter the HIPC process as agreed by extending the sunset clause.

PRGF – In our view, the ultimate goal of any PRGF arrangement is the graduation to a surveillance-based relationship. We support the introduction of a new shocks window within the PRGF and of the Policy Support Instrument for low-income countries. Furthermore, Germany will contribute to the subsidization of the Fund's Emergency Assistance for Natural Disasters. Together with the increasing use of low-access PRGF arrangements and higher multilateral debt relief, we expect less need for PRGF lending. However, it has to be ensured that the Fund continues to stand ready to assist low-income countries facing protracted balance of payments problems. We reiterate that the Fund's lending should be strictly confined to countries willing to implement ambitious reform agendas, with focus on mobilizing internal resources and setting up sound institutions.

IV. Other issues

Budget and staff compensation – For the next years, Germany continues to favor a constant administrative budget of the Fund in real terms. In order to achieve this, the Fund has to concentrate on core activities and management has to set clear priorities. We welcome the ongoing review of employment, staff compensation and benefits. We favor a simplified, transparent and rules-based system of salary adjustment, more financial incentives for the staff and a better performance-control for the management. The new system should ensure a Fund staff of highest quality with diverse nationalities and professional experiences and be consistent with the Board-approved Medium Term Budget Framework. Any significant changes in the current system may require some grandfathering.

Quotas, governance, voice and representation – Germany supports a fair representation of all members in the Fund, including developing countries. Quotas not only define the voting rights and the volume of possible Fund lending, but also the obligation to contribute to the Fund's financing mechanism, hence, bearing financial responsibility. Therefore, quotas should remain to be primarily determined by a member's relative weight in the global economy. However, we observe significant differences between actual and calculated quotas for a number of member states in each region of the world. For example, the actual quotas of many European members, including Germany, are lower than the calculated quota. Major imbalances could, for example, be adjusted by a redistribution of quotas. In our view, a quota increase for a member country also raises the expectation to assume broader responsibilities to the international community.