International Monetary and Financial Committee

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**Statement by the Honourable Jim Flaherty,
Minister of Finance, Canada**

On behalf of Antigua and Barbuda, The Bahamas, Barbados, Belize, Canada ,
Dominica, Grenada, Ireland, Jamaica, St. Kitts and Nevis, St. Lucia,
St. Vincent and the Grenadines

Washington, D.C., October 12, 2013

Statement Prepared for the International Monetary and Financial Committee of the Board of Governors of the International Monetary Fund

The Honourable Jim Flaherty, Minister of Finance for Canada, on behalf of Antigua and Barbuda, the Bahamas, Barbados, Belize, Canada, Dominica, Grenada, Ireland, Jamaica, Saint Kitts and Nevis, Saint Lucia, and Saint Vincent and the Grenadines

Since the last time we met, a number of important policy actions have helped to sustain the recovery, improve financial market conditions and strengthen private demand. However, global economic growth has disappointed with risks now more broadly spread throughout the global economy. The recovery is taking stronger root in most advanced economies while the slowdown in many emerging market economies is now projected to be deeper and longer than envisioned just a few months ago. Though this shift will present new risks and challenges, if sustained, it is also a welcome sign of strengthening and more sustainable growth in the economies hardest hit by the crisis. We are also reminded of the need to redouble efforts aimed at overcoming the impediments to stronger, more sustainable and balanced growth.

In its latest *World Economic Outlook*, the International Monetary Fund (IMF) rightly cautioned that without urgent policy action by major economies—both advanced and emerging—the global economy could settle into the current subdued growth trajectory over the medium term. We must move collectively and decisively to avoid such an outcome and create the conditions to increase growth and employment.

Our constituency members continue to face a diverse set of challenges and we are all carefully navigating the fragile recovery. In this Statement, I provide updates on economic developments and key policy priorities in the constituency relating to Canada, Ireland and the Caribbean. I also convey constituency views on key issues that affect the IMF's governance as well as its core role in safeguarding global economic stability through surveillance and adjustment lending.

Canadian Developments

Canada's economic performance over the recovery has been solid, reflecting Canada's sound economic, fiscal and financial sector fundamentals. Growth has been driven by a strong domestic economy, including robust business investment. As a result, Canada has more than recovered the business investment lost during the recession.

However, as I noted above, the global economic environment remains fragile, and Canada is not immune to these external developments. Growth in the euro area has only just returned to positive territory after six straight quarterly declines, and considerable risk remains over the region's implementation of needed reforms. In addition, uncertainty regarding U.S. fiscal policy in the short and medium term continues to be a risk.

The Government of Canada remains committed to returning to budgetary balance in 2015, and results to date indicate it is on track to achieve this goal. The Government has also announced, as part of its Group of 20 (G-20) commitment, a federal debt-to-GDP (gross domestic product) ratio target of 25 per cent by 2021. Recent policy actions aimed at achieving these goals include: initiatives to restrain the growth of direct program spending and improve the efficiency of government administration; measures to close tax loopholes and improve the fairness and integrity of the tax system; and steps taken to bring compensation for federal public servants in line with other public- and private-sector employees.

Economic Action Plan 2013 built on previously announced measures to create jobs, support growth and promote long-term prosperity. New measures include tailoring skills training to the needs of the labour market, a new 10-year Building Canada Plan for infrastructure investment, and new initiatives to support Canada's manufacturing sector and innovation. The Government of Canada has also recently begun implementing structural policies designed to increase Canada's long-term economic potential, including: reforming Canada's immigration system to ensure that it meets Canada's labour market needs; modernizing the regulatory system for major economic projects; launching a new approach to support business innovation; and improving incentives to return to work when unemployed.

Irish Developments

Ireland's economic performance this year is one of stabilization, with a welcome return to employment growth although GDP is being impacted by a series of one-off factors. Although real GDP fell by 1.1 per cent year-on-year in the first half of 2013, this is in large part due to structural change in the pharmaceutical sector (the well-known patent cliff), which has a large weight in Irish exports. Service exports, on the other hand, continued robust growth in the second quarter, reflecting competitiveness gains in recent years and the continuing attractiveness of Ireland for foreign direct investment.

High-frequency indicators from the third quarter are positive, including an increase in core retail sales and a return to modest growth in house prices after the sharp correction in evidence since 2007. It is, however, the labour market which has shown the most encouraging signs: employment grew by 1.8 per cent year-on-year in the second quarter. This is the fourth successive quarter of growth and is increasingly broad-based across sectors. Unemployment has fallen on an annual basis for four consecutive quarters and registered 13.4 per cent in August. While this is still unacceptably high, it is certainly moving in the right direction. Both manufacturing and service purchasing managers' indices are in strong positive territory and the nascent pick-up among Ireland's trading partners bodes well for Irish growth prospects in 2014.

The Irish authorities remain committed to the necessary fiscal consolidation. The robust performance of tax revenues in 2012 has continued into 2013 with tax receipts to end-August up almost 4 per cent year-on-year. Significant reductions continue to be achieved in the Exchequer deficit.

As Ireland's European Union (EU)-IMF Program of Financial Support, which began almost three years ago, runs to the end of this year, the Irish Government's focus has now firmly turned to exiting from the program. I understand that it is the Irish Government's intention to achieve a successful and durable exit from the program and a full and sustainable return to the financial markets. Ireland continues to meet the program conditions, with over 230 actions completed to date. The fact that Ireland is now in its fifth year of fiscal consolidation underlines the scale of the achievement. The strong implementation record has been recognized by the external partners and by the financial markets, as evidenced, for example, by the highly successful sale of long-term bonds, including a new 10-year benchmark, earlier this year. Irish government bond yields remain at historically low levels mid-September 2013, and this has been aided by arrangements around the refinancing of the promissory notes and the extension of the maturities of the EU loans. Ireland does remain vulnerable, however, to international developments.

The authorities are redoubling their efforts to address the remaining issues in the financial sector to ensure that it is well placed to service the real economy as it recovers. The authorities have built a very robust architecture, both structural and operational, to deal with the problem of mortgage arrears. A detailed analysis of the Irish banks' balance sheets is also taking place.

Returning to the real economy, the main challenge is to restore sustainable growth to address the pressing issue of high unemployment. The government is continuing its policy of seeking to promote pro-growth policy measures, such as through investing in infrastructure and through implementing reforms in education and labour market policies. Planning for growth is demonstrated by ongoing capital investment projects, such as in schools and roads, which are funded by a mix of Exchequer, European Investment Bank and public-private partnership funding.

Ireland held the presidency of the European Union during the first half of 2013 and good progress was made in key areas, such as the banking union and economic governance. Ireland agrees that the new European fiscal governance rules are an appropriate response to the challenges of recent years.

Caribbean Developments

In response to challenging circumstances, the Caribbean countries have been reforming their economies and strengthening their relations with the IMF and development partners to achieve this goal. Working with many departments and agencies such as the Caribbean Regional Technical Assistance Centre, the Caribbean countries have taken advantage of valued technical assistance and resources. Some countries are undergoing Fund-assisted programs and others are contemplating doing so to help arrest economic decline. Technical assistance, focused research and dialogue are invaluable ways in which the Fund can continue to support its smallest and most vulnerable members. These efforts, including the announcement of growth agendas coupled with strong fiscal consolidation programs, create the necessary fiscal space which is helping to lay the groundwork for a return to growth in the Caribbean. The financial sector has made considerable strides in undergoing significant reform to make it stronger and more resilient in the medium term. In addition, Caribbean countries have made some efforts to build infrastructure resilience to disasters to militate against the ever-present threat of climate change, which affects the very livelihood of citizens and tourism assets alike.

This notwithstanding, Caribbean economies are very slowly emerging from the global recession. Policy buffers are mostly depleted and sustained growth has proven elusive. Advanced countries, which are the main trading and tourism-generating markets of many Caribbean countries, have still not fully recovered, providing a challenge to the real sector. The best Caribbean performers continue to be those that have benefitted from strong commodity prices, but the tourismdependent countries have experienced only limited growth. Unemployment and debt levels remain high. Foreign exchange receipts are moderate, reflecting the narrow export concentration and a slowdown in economic activity.

Constituency Views on the IMF

Quotas and Governance Reform

I continue to believe that the IMF must have the appropriate tools and governance structure to promote global economic and financial stability. The landmark 2010 quota and governance reforms represent a very important step in the evolution of IMF governance. However, these measures have still not yet come into effect. We therefore encourage those members that have not yet ratified the agreement to redouble their efforts, as this delay risks slowing momentum on further progress in the 15th General Review.

Completing the 15th General Review of Quotas by January 2014 is an important step, including agreeing on a simpler and more transparent quota formula. Ensuring that this exercise results in an outcome whereby quotas are more closely aligned with members' relative weights and integration in the global economy remains our collective objective. We must also safeguard the voice and representation of the Fund's poorest and most vulnerable members.

The 15th General Review also presents an opportunity to assess the Fund's medium-term quota resource needs. It will be very important that this exercise be rigorous, underpinned by supporting analysis, and include a clear assessment of the institution's lending role and responsibilities relative to other partners. Equally important will be a more transparent distinction between the Fund's steady-state permanent resource needs and those needs that might arise in more isolated periods of elevated regional or global stress.

Surveillance and Advice

To help bolster the economic recovery and prevent the emergence of new crises, IMF surveillance and advice must continue to be high-quality, timely and relevant. Over the coming period, I encourage the Fund to examine how it can best maintain its focus on core risks and challenges at a time when the number of surveillance products and coverage within these exercises continue to expand. Boosting effectiveness and traction requires having IMF advice that is independent, candid and even-handed in order to promote confidence in the Fund's surveillance and advisory activities.

Traction also requires better tailoring surveillance and advice to the needs of members through more country-level specificity. This is particularly relevant for the IMF's engagement with its smallest members. Therefore, we welcome the progress that is being made to deepen the Fund's engagement with small states, a group that includes many countries in our constituency.

While the number and breadth of issues covered by Fund surveillance have multiplied, it is essential that the quality and depth of analysis of exchange rates and other external sector issues remain a priority for both multilateral and bilateral surveillance.

Lending and Program Design

I value the important role that the IMF has played in supporting its membership throughout the economic and financial crisis, whether in response to unforeseen shocks or deep-seated imbalances. Ensuring that the institution provides effective lending programs with appropriate conditionality that address the root causes of instability and provide a timely path to recovery and growth is a priority for our constituency.

Drawing lessons from recent crisis experiences is vital to identifying emerging trends and common warning signs. In this respect, upcoming reviews of the Fund's experience with large programs will be important, not only to further improve program effectiveness but also reassert IMF independence. The experience to date has been mixed. Some success has been achieved with respect to phased fiscal consolidation in program countries and external adjustment. However, the Fund has faced a number of challenges with respect to program design, including those that stem from overly optimistic growth and debt projections, and difficulties implementing internal devaluation. It is essential that the IMF have the flexibility to set the conditionality and design programs in a manner it sees as best for member countries, even when engaged with regional partnerships. The Fund's experience with some programs suggests that there is room for improvement in this area.

Finally, timely adjustment and exit from IMF support is also important given the revolving nature of Fund credit. Though the recent addition of new precautionary lending instruments has helped round out the Fund's lending toolkit, early experience has highlighted areas in need of adjustment. The way these instruments are currently structured, and experiences with them, suggest there may be insufficient incentives to exit precautionary arrangements, which are typically large and reduce funding available for countries with immediate financing needs. Therefore, as part of the upcoming review of these facilities, we also look forward to seeing a thorough examination of incentives to exit from them in order to ensure that IMF support always remains temporary.