International Monetary and Financial Committee

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**Statement by Minister of Finance Miroslav Kalousek,
in his capacity as Chairman of the EU Council of Economic and Finance Ministers**

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in his capacity as Chairman of the EU Council of Economic and Finance Ministers,
at the 19th Meeting of the International Monetary and Financial Committee
Washington, D.C., April 25, 2009

1. I submit, in my capacity as Chairman of the EU Council of Economic and Finance Ministers, this statement which focuses notably on the world economy, in particular the outlook and policies for the EU, and on IMF policy issues.

Economic Situation and Outlook

2. The global economy continues to face unprecedented economic and financial challenges. Global GDP declined rapidly in the fourth quarter of 2008, led by the advanced economies, and more recent indicators suggest marked declines also in the first quarter of 2009. Global trade has contracted dramatically, and financial markets remain fragile. The current situation is characterised by a large degree of uncertainty. Financial turmoil and low confidence contribute to a weak outlook. Nonetheless, very expansionary monetary and fiscal policies and actions to repair financial systems, as well as the real disposable income boost from lower commodity prices, contribute positively to the outlook.

3. In the EU, macroeconomic conditions worsened further at the start of the year. Household and business confidence is at an all time low but some indicators seem to be stabilising. EU financial rescue plans have averted the systemic risk of a general financial meltdown, but the provision of credit to the real economy is subdued and normal lending conditions have not yet been restored.

4. Inflationary pressures have moderated significantly in EU Member States, mostly reflecting a marked decline in energy and other commodity prices and the strong contraction of global demand. While there may a temporary period of negative inflation around the middle of this year in the EU as a whole, this will mainly reflect base effects. Inflation expectations beyond this horizon remain well anchored in line with the objective of price stability. Hence, there is no significant risk of deflationary developments for the EU as a whole.

Policy Responses to the Crisis

5. The EU developed a co-ordinated European response to the downturn through the European Economic Recovery Plan (EERP). The EERP, currently being implemented by EU Member States and the European Commission, focuses on supporting the real economy by coordinated fiscal impulses, contributing to the stability to the financial system, as well as external aspects.

a) Macroeconomic and structural policy response

6. Budgetary policies in the EU are providing an important support to aggregate demand and economic growth, appropriately differentiated among Member sates. Generally, Member States are allowing automatic stabilisers to play. The current extraordinary circumstances also justify targeted and temporary discretionary countercyclical measures with minimum adverse

side-effects, which should be consistent with the long-term sustainability objectives identified in the Lisbon Strategy, and include proper exit strategies reflecting the objectives of the Stability and Growth Pact.

7. The EERP aims to provide temporary support to the real economy and is expected to boost demand, generate new investments, create jobs and help the EU move to a low-carbon economy. Including automatic stabilisers, which are overall large in the EU, the total fiscal support amounts to at least 3.3 % of EU GDP in 2009 and 2010, or over EUR 400bn. Measures are targeted to stimulate demand by providing support for households, business, and employment, directly increasing demand through public investment and the modernisation of infrastructure. Most of these measures are consistent with the longer-term objectives identified in the Lisbon Strategy for Growth and Jobs – such as building Europe's knowledge base and boosting energy security.

8. The inflation outlook has allowed monetary policy to be eased substantially by the ECB and national central banks, including through lower rates, ample liquidity provisions, and unconventional policy measures.

9. In the months to come, it will be important to focus on the implementation of the stimulus in a timely, targeted and - where appropriate - temporary manner, while respecting fiscal sustainability in line with the Stability and Growth Pact and the openness within the Internal market and vis-à-vis third countries, ensuring non-discrimination of products and services within the EU, and ensuring consistency of short-term measures with long-term reform objectives.

10. The EU stresses the need for a global cooperative response to the current crisis and call on its partners to refrain from competitive devaluation of their currencies and to promote a stable and well functioning international monetary system.

b) Financial market policy response

11. Since autumn 2008, financial sector rescue operations have been carried out in EU Member States and measures are being taken to stabilise the financial system and to improve financial governance.

12. As the real economy has weakened, the fragility of the financial system has been further exposed, which has contributed to a further decline of economic activity. This interaction could lead to a vicious circle of financial stress and decelerating output growth. A key priority on the international agenda is therefore to break this vicious circle and continue the efforts to restore confidence in the markets. Government measures should be implemented on a timely and coordinated basis, as spelled out in the framework of the G20 process. Priority tasks include:

- Restoring the functioning of credit markets and facilitating the flow of lending to the real economy. Measures to restore the full functioning of the financial sector and in particular the banking sectors, must be implemented on a timely and coordinated basis, safeguarding the level playing field. There is also a need to prepare a strategy for the authorities to exit from interventions as soon as market conditions return to normal.

- Establishing a comprehensive, ambitious and globally coordinated approach towards regulatory reform, ensuring that all financial products, institutions and markets are appropriately regulated and subject to oversight. The financial regulatory and supervisory environment will be overhauled to prevent future crises, mitigate moral hazard, and reduce the need and potential cost of public interventions.

- Improving the cooperation between financial authorities at international level. There is a need to better supervise globally large complex financial institutions, including through supervisory colleges and strengthen the collaboration between the IMF and the FSB (Financial Stability Board, previously Financial Stability Forum) to identify risks and vulnerabilities to global economic stability at an early stage.

- In October 2008, the European Council agreed to the co-ordinated implementation of national measures to support the financial system with the objective of: (i) averting the immediate threat to financial stability and the banking sector in particular; (ii) promoting a return to normal functioning in the interbank and other wholesale credit markets; and (iii) underpinning lending to the private non-financial sectors of the economy, and thus mitigating the effects of any credit supply constraints. Several Member States have announced and implemented measures, including (i) state guarantees for bank liabilities; (ii) recapitalisation through direct capital injections into financial institutions; (iii) increased access to liquidity from central banks; and (iv) addressing the problems caused to financial stability by impaired assets. The European Commission has approved several individual bank rescue plans within the context of state-aid rules and provided guidance which aim at: (i) minimising the economic and budgetary cost of state-aid intervention; (ii) minimising the inherent competition distortions between banks and Member States; and (iii) guaranteeing the functioning of the internal market.

As to the future regulatory reforms, the following specific proposals should be pursued:

- The strengthening of financial regulation should include a stronger, more coherent supervision framework. At the European level, the de Larosière Report has made proposals which will be the basis for reforming the EU supervisory framework.

- Decisive action should be taken to mitigate the inherent pro-cyclical nature of the financial system. This should include reviewing which tools are most appropriate and strengthening the use of dynamic provisioning and capital buffers, as well as reviewing rules concerning compensation schemes in the financial sector and ensuring that they are effectively enforced (e.g. via prudential rules). In particular, accounting standard setters should work closely with prudential supervisors and regulators to improve valuation and provisioning practices and achieve a single set of high quality global accounting standards.

- The implementation of Basel II at international level is of key importance to ensure that banks hold an adequate level of capital to withstand and absorb losses. Once the recovery is assured, these capital requirements should be further strengthened over time, to increase the quality, quantity and international consistency of prudential capital, as well as to improve risk coverage of the requirements. Excessive leverage should also be tackled.

- Credit rating agencies should be subject to mandatory registration and supervision, in order to ensure the integrity of both the rating process and the ratings themselves.

- Hedge funds and private equity activities have come under increasingly sharp international scrutiny. Regulatory initiative on hedge funds should in particular be based on the assessment of systemic risks, their contribution to overall leveraging, the need to preserve market integrity, efficiency and transparency towards counterparties and investors, as well as investor protection. It should be ensured that hedge funds or their managers will be registered.

- Derivative markets should be subject to greater transparency. There is an urgent need to establish well capitalized and well managed Central Counterparties (CCPs) subject to effective regulation, and supervised with high prudential and operational standards.

- Remuneration schemes in the financial sector should not induce excessive risk-taking in financial institutions and should promote the long term sustainability of financial institutions. Any compensation arrangement would need to be backed-up by effective supervision and enforcement.

- Non-transparent and non-cooperative jurisdictions, including off-shores centres, should be subject to financial regulation and supervision in order to guarantee financial stability.

c) Contributing to a more favourable international environment

13. Global imbalances remain a medium-term challenge for global macroeconomics and financial stability, including the risk that the world economy returns to a growth path without having substantially corrected underlying imbalances. Developments related to the current crisis, as much as they reflect more than mere cyclical adjustments, are contributing to reducing global imbalances. Despite this correction, global imbalances remain large and all major countries and economic areas have to play their part to resolve them in a manner compatible with sustained global growth, including by continuing to implement the agreed strategy adopted in the context of the Multilateral Consultations on Global Imbalances. The IMF should take into account this dimension throughout its surveillance activities.

14. Markets should be kept open and all forms of economic protectionism avoided. Implementing the commitments agreed at the April 2009 London summit not to impose new trade restrictions and not to create new subsidies to exports is essential. Given the drastic deterioration in industrial production and decrease of trade around the world, there is a need to re-affirm that it is in our mutual interest to support trade by promoting the orderly supply of trade financing, and to avoid competitive devaluations and anticompetitive measures. The EU strongly supports a multilateral initiative to mitigate the decline in trade finance provided by the private sector.

15. On international trade policy, the EU remains fully committed to constructively pursuing the Doha negotiations with a view to reaching an ambitious, balanced and comprehensive agreement. Maintaining and strengthening the multilateral trade system based on the WTO is of key importance for growth and employment prospects of the global economy, as well as for development.

16. An effective, efficient and equitable response to the challenges of climate change and its economic consequences require international collective action. Through an integrated and harmonised approach to climate and energy policy, based on cost-effectiveness, competition, diversification of sources, subsidiarity and cooperation between Member States, the EU is

committed to transforming Europe into a highly energy-efficient and low greenhouse-gas emitting economy. In most of the world energy use is much less efficient than in the EU, due to inter alia inappropriate oil and carbon pricing and regulation, and there is substantial scope for increasing energy efficiency and avoiding waste, while at the same time reducing emissions, improving energy security and enhancing economic development. Actions to reduce our reliance on fossil fuels must not endanger global food supply, and should not be distorted by government subsidies. The development of emissions trading and the creation of a global carbon market can play a powerful role in achieving cost-effective emissions abatement. A key challenge in promoting environmental sustainability will be to ensure that this transition to a low-carbon economy is handled in a way that is consistent with sustainable development, competitiveness, security of supply, as well as sound and sustainable public finances. All countries should contribute to a successful outcome of the UN Climate Change Conference in Copenhagen based on the principle of common but differentiated responsibilities and respective capacities.

IMF Policy Issues

17. EU Member States welcome the efforts undertaken by the IMF over the last months in adjusting its institutional and financial set-up to ensure that it can assist members effectively in the current extraordinary global economic and financial environment. They recognise that further reforms regarding its mandate, scope and governance will be warranted to strengthen the IMF so that it better meets the needs of its membership and fully addresses the challenges posed to the global economy in the 21st century. EU members will continue to contribute constructively in this process.

IMF resources

18. EU members support a very substantial increase of IMF resources to fulfil the financing need identified by the IMF to counter the adverse effects of the financial crisis and to support growth in its member countries, and are ready to take their part. The increase of resources should be implemented through increasing and enlarging the NAB, and EU members urge other countries, in particular those that over the last years have accumulated significant international reserves, to contribute in order to achieve a fair burden-sharing among IMF members. All countries participating in the NAB should ratify changes swiftly. As for timing reasons transitional arrangements in form of bilateral loans are needed, these bilateral agreements should be implemented in a transparent way and should be compatible with the NAB so that they could be easily embedded into the NAB. In this context, EU Member States will provide a fast temporary support of the SDR-equivalent of EUR 75bn on aggregate, on the basis of standardised agreements.

19. EU Member States urge all IMF members who have not yet done so to ratify the Fourth Amendment to the Articles of Agreement. In parallel, they support a general SDR allocation and call on the IMF to come forward with a detailed assessment of such a scheme and a proposal on how to implement it, including a review of the likely implications for different groups of countries and for the international monetary system. Given that at this juncture the long-term need for global liquidity is difficult to assess, the inclusion of a review clause would be useful.

20. EU members recall that the EU has contributed substantially to recent IMF lending programmes (Hungary, Latvia, Romania), both through the Community's Medium-Term Financial Assistance Facility and on a bilateral basis. The facility's ceiling has recently been

doubled to EUR 50bn demonstrating the EU's commitment to continue to contribute to the resolution of the current crisis. They welcome the close cooperation with the IMF in designing the programmes.

Surveillance framework

21. The economic and financial developments in the last months underline the relevance and the need of effective surveillance for the proper functioning of the global economy. In this context, EU members support a further strengthening of the IMF's surveillance, both the bilateral and multilateral dimension, with a view to strengthen its role in crisis prevention, and to improve and reinforce surveillance of the financial sector. The EU supports an IMF surveillance of all economies and financial sectors, of the impact of policies on others and of risks facing the global economy. Also, there is a need to increase the commitment of IMF members towards IMF policy recommendations, as well as to ensure independent IMF policy analysis, and to foster transparency and even-handedness, leading to genuinely effective IMF surveillance.

22. EU members support overall assessments of the vulnerabilities of IMF members' financial sectors through regular implementation of Financial Sector Assessment Programs (FSAP), in particular for all systemically relevant countries, and a better integration of financial sector surveillance in Article IV reports.

23. The collaboration between the IMF and FSB should be enhanced to identify macro-financial risks at an early stage, with regular reporting to the IMFC. EU members welcome the pilot joint Early Warning Exercise, which will contribute to identifying systemic risks and weaknesses arising from the financial sector and regulation.

Lending framework

24. EU members welcome the review of the IMF's facilities, conditionality and charges undertaken over the last months. The reform adopted by the IMF Executive Directors in March leads to a far-reaching streamlining and adjustment of the IMF's lending framework, and the IMF's toolkit for assisting members in preventing and resolving financial crises has been strengthened. In this context, EU members welcome the elimination of the Supplemental Reserve Facility, the Compensatory Financing Facility and the Short Term Liquidity Facility.

25. Also, EU members welcome the agreement reached in the IMF Board on the Flexible Credit Line (FCL) which strengthens the IMF's capacity to prevent and respond to crises. In the current global economic environment the creation of the FCL is an appropriate response to provide high and rapid access to IMF resources for members with strong policies and economic fundamentals. The FCL must be implemented in a coherent and responsible way, ensuring an effective early involvement of the Board and relying on a rigorous and transparent qualification framework, in order to safeguard IMF resources, including for non-precautionary lending. The review clause included in the FCL decision will be useful in this respect.

Role of the IMF in low-income countries

26. Low-income countries (LIC) are hit hard by the global financial and economic crisis. As they are in a weak position to adequately respond with domestic means, stepping up

international support is required to support macroeconomic and financial stabilization of these countries.

27. EU members welcome the review of the IMF's instruments for LIC aimed at ensuring that they better meet members' needs. They welcome the agreement to double access limits for concessional financing. This will make financing to LIC more flexible and will contribute to alleviating the impact of the global financial crisis on the poorest economies, and to preserve the development progress made over the last years.

28. EU Member States stand ready to work on the IMF proposals to mobilise additional resources, consistent with the new income model, including from agreed sales of IMF gold, to provide – on top of bilateral financing - additional concessional and flexible finance for the poorest countries.

29. The IMF, consistent with its mandate, should continue helping LIC to achieve and maintain macro-financial stability and sustainable economic growth. EU members underline the importance of close collaboration with development partners, notably the World Bank, drawing on the institutions' different expertise.

30. EU members reaffirm the importance of applying rigorously the debt sustainability framework. A differentiation of new borrowing conditions with respect to the risk of debt distress assessed in the debt sustainability analysis should not lead to a weakening of the framework.

Governance reform and IMF mandate

31. EU members call on all IMF members to swiftly ratify the reform of quota and voice agreed in April 2008. They support a conclusion of the next quota review by January 2011.

32. EU members remain committed to strengthening the effectiveness and legitimacy of the IMF by enhancing governance and ensuring that economic weights in the world economy are adequately reflected. They will contribute constructively towards finding appropriate responses in order to improve the functioning of the IMF. EU members take note of the report by the Manuel Committee and the work underway in other groups on possible reform options. IMF governance reform involves complex and difficult questions that will require thorough discussions. Such a reform should be comprehensive and broad-based, including reviews of the IMF's corporate governance and of decision-making rules, as well as the IMF's mandate. EU members are ready to explore the inclusion of capital account surveillance into the mandate.

33. EU members support a merit-based and transparent process for the selection of the senior management, both for the IMF and the World Bank, irrespective of nationality.

Non-cooperative jurisdictions

34. EU countries remain strongly committed to reinforced action towards uncooperative and non-transparent jurisdictions that lack compliance with agreed international standards in the areas of taxation, prudential supervision and money laundering, counterfeiting and terrorist financing. They support the listing of such jurisdictions, and the development of a toolbox of sanctions that permits the application of appropriate and gradual countermeasures.