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Statement by Mr. Paulson

U.S. TREASURY DEPARTMENT

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STATEMENT BY
U.S. TREASURY SECRETARY HENRY M. PAULSON
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SINGAPORE

Today's IMFC meeting underscores the central importance of the IMF moving forward rapidly to modernize itself and meet the demands of an ever-changing global economy.

We are fortunate to be able to make these reforms from a position of strength, as the world economy continues to expand at a solid pace. We must, however, remain vigilant as the outlook faces potential downside risks from protectionist forces, disparities in economic performance, and tight energy markets.

Trade liberalization is a vital component of our agenda and the suspension of the Doha Round represents a huge disappointment. The global community simply must resist the forces of protectionism and isolationism. Each delay in our efforts to achieve an ambitious result in Doha robs the world – in particular the poor countries and the poor among us – of new opportunities for growth and development. The World Bank estimates that full liberalization of merchandise trade would increase annual global income by $287 billion (0.7 percent of global GDP) and lift 65 million people out of poverty by 2015. The United States remains fully committed to achieving a successful outcome, but others – both developed and developing countries – must also play a leadership role in getting the round back on track. The IMF can also continue to help through its strong advocacy of trade liberalization, as well as specific contributions such as the Trade Integration Mechanism and technical assistance for customs and tax reform.

The U.S. economy remains strong. Real GDP growth rose 3.6 percent in the last four quarters and is settling into ranges more in line with our long term potential. Strong productivity growth, at 3.2 percent per annum since 2001, has underpinned this success. The labor market is strong: since August 2003, the economy has added more than 5.7 million jobs. Inflation is moderate – while consumer price inflation is running at 4.2 percent, stripping out energy and food costs, core consumer price growth is only 2.7 percent over the past 12 months. The U.S. economy's high degree of openness is a key source of its strength and its attractiveness as a location for investment.

The international community has an agreed strategy to reduce global imbalances in the context of maximum sustained global growth. Progress depends on vigorous action by all parties. The United States is doing its part. The U.S. economy has long been an engine of global growth. The U.S. is steadily shrinking its fiscal deficit thanks to a strong economy and correspondingly strong tax receipts. Many analysts project that the federal deficit will be 2 percent of GDP this year. It appears we will meet the President's goal to halve the deficit a year ahead of schedule. However, others must also do their part. Without structural reforms in major surplus countries and Europe, greater exchange rate flexibility in Asian emerging economies, and increased capacity investment by oil exporters, large imbalances will simply persist.

Progress on IMF Reform

The United States firmly believes that that the international system needs a strong and effective IMF. To ensure its continued centrality, we must together modernize the IMF and act swiftly to implement an ambitious reform agenda.

The IMF's current governance structure reflects policies put in place in the 1960s and 1970s. But the world economy has changed. Private capital flows predominate. Many fast-growing emerging markets are playing an increasingly prominent role in the world economy, while performance among others has lagged.

The IMF's governance must be overhauled. We welcome the two-stage proposal to launch and achieve long overdue and fundamental reform in the current quota system. For the IMF to remain relevant, it must reflect the economic weight of fast-growing emerging markets such as China, Korea, Mexico, and Turkey. These four countries are underweight by any reasonable measure and will benefit from an ad hoc quota increase in the first stage.

But this first stage is a small down-payment against an even more important second stage aimed at promoting fundamental reform. In particular, the IMF needs a new, simplified quota formula with GDP as the dominant variable. We seek this change not to help the largest economies – the United States is firmly on record that we will forgo any share increase in the second stage beyond current levels – but to recognize emerging economies, which have achieved fast growth. Indeed, we challenge other industrial countries to join the United States in forgoing higher voting shares in the second stage. We must also act to ensure another round of ad hoc quota increases on the basis of the new formula, which achieves significant reduction in out-of-line quota shares. The United States strongly believes in the imperative of an appropriate voice for the poorest countries, especially in Africa, and supports at least a doubling of basic votes to protect low-income countries' current shares. We hope the membership can agree and implement these reforms quickly – preferably by the time of next year's Annual Meetings.

Reforming the IMF's governance structure will not suffice. In revitalizing the IMF, we must also improve the Fund's effectiveness. First and foremost, this requires strengthening exchange rate surveillance, the Fund's most fundamental responsibility. This is particularly relevant for those currencies that do not yet trade in open, competitive markets. We should immediately revise and update the IMF's 30-year-old guidelines on exchange rate surveillance. The 1977 Surveillance Decision should be rewritten to better define acceptable country-specific exchange rate policies and practices. This includes considering the consistency of exchange rate policies with the international system and investigating misaligned currencies regardless of intent. Examining whether sterilization impedes external adjustment would also assist in promoting a better functioning international system. Of course, exchange rate policies must be considered in the context of monetary, fiscal, and financial sector policies and conditions.

Once these revisions on foreign exchange surveillance are completed, the Fund should rigorously implement the new guidelines. The IMF houses great technical expertise, capable of carrying out this task. But if the Fund does not do the job, pressures will mount on individual countries to do so to the detriment of all countries.

We welcome the IMF's continued engagement to design a contingent finance facility to help emerging market countries defend against external shocks. More work is necessary to balance the need to safeguard IMF resources with giving users the predictability and scale of access that they desire. We look forward to considering additional IMF work on whether a facility that meets these criteria can be designed. The development of sound financial markets is another critical element of the IMF's work on crisis prevention. The new Monetary and Capital Markets Department should take up the task of improving the IMF's understanding of market developments and their implications for economic growth and stability.

The IMF continues to have an important role in low-income countries, but low-income members are best served if the IMF limits its focus to short-term balance of payments lending and policy dialogue/technical assistance in its core areas of fiscal, monetary and exchange rate policy. The IMF has undertaken useful work on the macroeconomic impact of aid flows and has a key role in helping low-income members manage the impacts of the scaling up of development aid. The advice of the External Review Committee on the division of labor between the Fund and Bank will be helpful. Following on the achievements of the Multilateral Debt Relief Initiative (MDRI), further work is needed to establish incentives to deter the rapid re-accumulation of debt for post-MDRI countries and address the free rider problem.

The Fund has seen a steep drop in credit outstanding over the past year, which impacts Fund finances, but it is premature to take decisions to fundamentally alter the way the Fund is financed, especially if they may loosen the IMF's budget constraint before giving greater thought to the appropriate role and size of the Fund in a world of reduced demand for its lending. The IMF's reserves remain ample to cover expected shortfalls in the interim.

Protecting the financial system from abuse by terrorists and illicit financiers is integral to international financial stability and global security. We must aim for closer bilateral and international cooperation to identify and disrupt the support networks of these international security threats, including through the reporting and sharing of financial information. Financial intelligence is among our most valuable sources of data for waging this fight, and finance ministries and central banks play a pivotal role by drawing upon financial information to detect and disrupt terrorist and illicit money flows. The work of the IMF and World Bank is instrumental in fostering implementation of the international AML/CFT standards, and we call for deepening cooperation with the FATF.

Thank you.