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On behalf of Austria, Belgium, Belarus, Czech Republic, Hungary, Kazakhstan, Luxembourg, Slovak Rep., Slovenia, Turkey
The Global Economic Outlook

Signs of economic stabilization are appearing in many regions. Global policy coordination, fiscal stimulus measures, public support for the financial sector, and significant potential and actual financial assistance from the IMF and other international financial institutions have yielded good results. Improved confidence and a turn in the inventory cycle have created the opportunity for a more sustained recovery. However, policymakers cannot be complacent.

So far, the factors behind the upturn are mainly temporary. Rising unemployment and reduced wealth after the assets price bust will continue to affect consumer confidence and demand in advanced economies. Rising credit losses and deleveraging of banks’ balance sheets may reduce access to capital for private sector investment. We agree with the analysis of the Fund that in advanced economies the recovery may be sluggish, and thereby affect emerging market economies that rely on exports to advanced countries.

Premature withdrawal of supportive fiscal measures should be avoided as this could harm the recovery. However, rising borrowing costs and crowding out of private investment should be eschewed by adopting credible fiscal adjustment strategies that respond adequately to the upcoming costs of an ageing population in advanced countries. In the European Union, the Stability and Growth Pact provides a solid and credible framework for fiscal consolidation.

Economic integration increases interdependence and spillovers of national policies on other countries. Country specific factors, the stage of the business cycle, the public debt structure, and the size of fiscal multipliers will determine a country’s timing for withdrawing fiscal stimulus, central bank liquidity, and financial sector support. All types of protectionism should be avoided. International cooperation and Fund advice should help avoid undue distortions in competition and spillovers from policy measures that are not fully synchronized but tuned to individual country circumstances. The decoupling of major central banks’ interest rates may create unwarranted exchange rate volatility and the emergence of significant carry trade.

Cyclical factors have reduced global imbalances. Most economies are facing a period of slow growth, with mutually reinforcing factors depressing demand. When the recovery takes hold, savings in the private and public sectors of deficit economies, like the US, should be promoted. This will help contain global imbalances.
Asian surplus economies for now have replaced faltering external demand by stimulating domestic demand through comprehensive stimulus packages. China, in particular, has seen a significant rise in domestic demand. The increase in fixed investment was even higher, implying risks of a build-up of overcapacity, creating new vulnerabilities. Buoyant credit growth should be monitored closely. In the medium term, balanced growth necessitates higher domestic consumption, which could be fostered by strengthening social safety nets. A well-functioning financial infrastructure will provide more optimal capital allocation on the basis of market signals. We welcome the recognition by emerging Asian surplus economies that changes to their growth model are necessary.

In some emerging market countries, the threat of inflation, inter alia because of highly expansionary fiscal policies, requires increased attention. Rigid exchange rate arrangements could pose a threat to financial stability in these economies. Stability of capital flows to emerging markets should be promoted.

Financial Markets

Global financial markets have stabilized and systemic risks have been reduced. The unprecedented, and in some cases concerted interventions in advanced economies have helped in averting a collapse of the financial system. Access to IMF financing and bilateral credit lines between central banks that provided foreign exchange liquidity have also played a critical role. The encouraging signs of recovery, although still fragile, have provided a much welcome support to weak market confidence. Financial institutions have made important progress in recognizing losses and strengthening their capital base.

There is still a high risk that adverse developments in the real economy will affect the financial sector. Rising unemployment and a weakening commercial real estate sector continue to put pressure on the banks’ balance sheets. The deleveraging process in the banking sector might drag the economic recovery as credit supply diminishes. Securitization markets, which drove the credit expansion in the pre-crisis period, have not yet fully reopened. This requires that securitization becomes more transparent, less complex, offers significantly better guarantees for proper risk management, avoid conflict of interest, and can rely on highly liquid secondary markets.

Low interest rates in the past years have contributed to excessive leverage and risk taking. Central banks should closely monitor financial sector behavior and asset price movements. Central banks should when appropriate compliment their interest rate decisions with macroprudential measures to help preserve financial stability.

Authorities must stand ready to provide support to the credit markets. Recapitalizing banks, preferably with core capital injections, is critical for adequate credit supply.

Sound and stable financial intermediation requires a regulatory overhaul to curb excessive risk taking that triggered the recent financial crisis. The absence of well-designed strategies to contain the ramifications of the failure of systemically important financial institutions accelerated during the crisis the sharp fall in market confidence, if not panic. We support the ongoing work of the Fund, in cooperation with the G20, the BIS and the FSB, on a framework which will enable the
national authorities to identify, assess and address systemically important institutions, markets and instruments. A “too-big-to-fail” status increases moral hazard risks that should be addressed.

The IMF’s Crisis Response and Reform Agenda

The IMF continues to be the best equipped institution to foster international monetary, economic and financial cooperation. Its legitimacy is anchored in a formally binding international agreement and its universal membership. History shows that multilateral coordination is essential not only during crises but also in good times and during recoveries.

Surveillance

In line with the Fund’s mandate, surveillance should guide the institution’s universal membership in policy design and coordination toward a sustained and balanced recovery.

The Fund has made good progress in implementing the priorities identified in the 2008 surveillance review. Bilateral surveillance should further focus on cross-country spillovers. An in-depth review of the state of a country’s financial sector, whether supervisory regulation and practices are adequate, the extent to which its financial sector is vulnerable to macroeconomic shocks and how fragilities in the financial sector endanger internal and external macro-economic stability, are integral parts of the Fund’s surveillance mandate.

We welcome the revised operational guidance of the 2007 Surveillance Decision and urge all members to comply with the consultation obligations under Article IV.

We invite the Board to explore further the inclusion of capital account surveillance into the Fund’s mandate.

The analysis in the early warning exercise of risks and vulnerabilities surrounding the baseline scenario should feed into Fund’s surveillance. A proper division of labor with the Financial Stability Board is important.

We look forward to work by the Board on making the surveillance process more efficient.

Lending by the IMF

The Fund should continue to assist its member countries deal with actual or potential balance of payments needs while safeguarding its own resources. The experience in recent months shows that the Fund’s lending framework works well.

We should make sure that the Fund has sufficient resources in the longer term. The Fund is a quota based institution and borrowing cannot be a substitute for quotas. Fair burden sharing is important in raising resources. We look forward to the expansion of the NAB.
The Fund’s GRA resources cannot be used for subsidizing operations. The reimbursement to the GRA of its administrative expenses, relating to the PRGF-ESF Trust, is an integral part of the new income model.

*Low-income countries*

We welcome the simplified concessional lending framework for Low-Income Countries. Poverty reduction and growth should remain at the centre of the Fund’s assistance to low-income countries. Greater ownership of programs will foster better program implementation and efficiency.

The lending capacity of the PRGF-ESF Trust must be increased to help many low-income countries that face severe balance of payment problems because of the global financial crisis. More expansionary counter-cyclical fiscal policies might be appropriate when countries face major shocks such as in recent years. However, it must be ensured that such policies as well as higher access to financing provided by international financial institutions do not endanger debt sustainability.

We support the more flexible approach on concessionality as it is firmly anchored in the Fund’s Debt Sustainability Analysis.

*SDR*

We support the staff’s efforts to expand the network of standing two-way arrangements with individual SDR holders. These voluntary arrangements have greatly facilitated transactions in SDRs. Fair burden sharing among financial transaction plan members is desirable. The way countries use their SDRs should be monitored by the Board. If patterns of unbalanced use would appear, a reconstitution obligation should be considered. The Board should regularly review whether a change in the size of allocated SDRs would be warranted, in view of the global outlook and a reassessment of the global need of reserves at that time.

*Governance*

The IMF has a unique governance model. It is fair to conclude that the Fund’s governance is relatively effective and efficient, particularly in comparison with other international institutions. We welcome the report by the Executive Board on Fund Governance.

We call on all IMF members to swiftly ratify the reform of quota and voice agreed in April 2008. This is particularly important given the intention to reach agreement on the next quota review by January 2011. We look forward to the 2008 data update. The fourteenth general quota review should lead to a significant increase in actual quota shares of underrepresented countries, most of them being emerging market and transition countries, on the basis of the existing quota formula.

We support the aim to get more political involvement from all country authorities and the proposals to strengthen the IMFC.
We support a merit-based selection of senior management without geographical preferences. The political independence of the Managing Director and the staff is essential.

There is no reason to change the responsibilities of the Board and Management. The Board should focus on strategic issues and effective overview.

The current size of the Board strikes the right balance between effectiveness and inclusive representation. We are open to consider changes in the special voting majorities.