



International Monetary and Financial Committee

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**Statement by Wolfgang Schäuble
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On behalf of Germany

Statement by Mr. Wolfgang Schäuble
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to the International Monetary and Financial Committee
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I. Introduction

First of all, I would like to thank the Japanese authorities for their outstanding hospitality and the excellent organization of these Annual Meetings here in Tokyo. We cordially welcome the Republic of South Sudan as a new IMF member.

II. Global Economy and Financial Markets

Global Economy

The global recovery is progressing at a moderate pace and risks to the outlook are considerable. Our main task at the current juncture is to rebuild confidence. Fiscal consolidation and the deleveraging process of banks, firms, and households continue to dampen growth in the short-term. However, delaying necessary adjustments would further aggravate risks for the prospects of a lasting, fundamentally sound global recovery. Fiscal and financial sector adjustments are crucial to regain lost credibility and strengthen confidence. While international cooperation is important, decisive commitment and policy implementation at the level of individual countries is the most powerful lever. Growth-oriented fiscal consolidation with ambitious structural reforms will restore market confidence and improve the conditions for growth. In Europe, we will implement the stronger fiscal framework as agreed. Other major advanced countries should also implement sustainable fiscal consolidation plans rapidly.

For the euro area the growth outlook for 2013 appears weaker than previously expected. However, significant progress has been achieved in fiscal consolidation over recent years, thereby fostering the foundation for future growth. From 2009 to 2011, euro area countries, on average, reduced the deficit-to-GDP ratio by 2.3 percentage points. Fiscal adjustment in the euro area is continuing in 2012, and it is indeed crucial that efforts are maintained to restore sound fiscal positions.

Some progress in restoring international competitiveness has already been made. Unit labor costs and current account balances have started to undergo a correction process in most of the countries that have been strongly affected by the crisis. The initiated structural reform processes in the labor market and other areas start to yield tangible results. Further structural reforms are essential for euro area countries to strengthen competitiveness, increase the flexibility of their economies and enhance longer-term growth potential.

Germany

In 2012, the German economy remains one of the growth drivers of the euro area. Domestic demand – driven by increasing employment and wages – made the largest growth contribution in the last two years. Thus, Germany also contributes to a gradual, market-driven unwinding of global economic imbalances.

The labor market situation in Germany is projected to remain favorable, although the upward trend in employment has been flattening recently. Unemployment is likely to stay below the three-million mark on average, both in 2012 and 2013.

Altogether, Germany's economic upturn is expected to continue, but at a more moderate pace, with growth perspectives dampened by the European debt crisis and an overall global slowdown. Therefore, resolving this crisis remains of utmost importance. Regaining sound and sustainable public finances is key to restore confidence and growth in Europe and the global economy.

Germany remains firmly committed to a growth-friendly consolidation strategy contributing to restore trust in the euro area. We have successfully met the requirements of our constitutional "debt brake" as well as the requirements at the European and international level – and we will continue to do so in the future. In the 2012 budget and the financial plan until 2016, the Federal Government's net borrowing falls well below the maximum permissible net borrowing. We aim at a general government deficit of about ½% of GDP in 2012 and a nearly balanced budget by the year 2014.

Financial Sector

Stress in financial markets has receded, also following the ECB announcement of the OMT. Recent signs of stabilisation are welcome, but remain fragile. It is now of utmost importance that those members of the euro area which are still vulnerable demonstrate an unwavering commitment to economic reform. Significantly decreased sovereign risk premia over the last months for Ireland and Portugal indicate that markets see a significant difference in fundamental risk. And they expect to see determined reforms, based either on program conditionality or on a clear political commitment, and they will acknowledge progress.

Another important aspect is the valuation of banks: Price-to-book value ratios of European banks have been declining substantially and are far below 1 now (0.5 as opposed to around 2 before the crisis). Markets apparently doubt the profit prospects of the sector signaling that the repair of the banking sector is far from complete. Losses have to be absorbed, deleveraging has to take place, and further bank restructuring lies ahead. As banks search for profitable business, new risks are likely to emerge.

Hence, a strong, convincing single supervisor in Europe will be important. The retrenchment to core businesses and national markets is a normal reaction to financial crisis. Some of this is structural, as banks are adapting strategic priorities and business models. And some of it is

driven by uncertainty and risk aversion. This underlines the importance to regain confidence in the banking sector of particular euro area countries by cleaning-up of the balance sheets. This should be accompanied by the establishment of an effective European supervisor in order to foster a sustainable return to financial market integration.

III. International Financial Architecture and IMF Policies

IMF Resources

It is of utmost importance that the IMF has sufficient resources to fulfill its systemic role. Germany has committed to contribute EUR 41.5 billion to a new round of bilateral credit lines to temporarily increase resources in the IMF's General Resources Account as part of a broad international effort. The Deutsche Bundesbank has already approved the respective bilateral loan agreement with the IMF which is being signed on the occasion of this Annual Meeting. We call on other countries and central banks that also have made such bilateral pledges to the IMF to finalize their bilateral financing agreements with the IMF soon so that all financial contributions committed at the Los Cabos G20 Summit become operational. Our understanding is that any bilateral borrowing by the Fund is temporary and only a second line of defense after quota and NAB resources while the IMF should remain a quota-based institution.

The doubling of quotas in the context of the implementation of the 2010 decision on quota and governance reforms will contribute to a rebalancing of borrowed resources in relation to quota resources. This will bring the provision of financial means closer in line with the governance structure of the Fund, which will also enhance its legitimacy.

We emphasize the need for prudent financial policies and appropriate risk mitigation measures, in particular access, conditionality and adequate program design, to safeguard the Fund's resources. Furthermore, as part of the strategy, strengthening the Fund's precautionary balances must be given high priority and we call for a timely review.

IMF surveillance

Surveillance is the primary tool for the International Monetary Fund to fulfill its important crisis prevention function and remains the core competence of the IMF. Germany welcomes the recent adoption of the new surveillance decision which will contribute to a better integration of bilateral and multilateral surveillance, not least by facilitating a more systematic coverage of all relevant spillovers. This decision provides comprehensive guidance on the scope of the Fund's multilateral surveillance mandate to ensure the effective operation of the international monetary system. Furthermore, the decision rightfully emphasizes the importance of domestic policies that aim at preserving domestic stability as an indispensable precondition for and essential contribution to safeguarding global stability. By the same

token, for these economies facing inward spill-overs, it is all the more important to consistently reduce home-grown vulnerabilities.

In addition to these steps a timely implementation of the other findings of the 2011 IEO study on the Fund's surveillance is of great importance to further enhance the quality and relevance of the important surveillance function of the Fund.

Germany also welcomes the Fund's ongoing efforts to enhance its financial sector surveillance and the recent adoption of the financial sector surveillance strategy. To take the interconnections among countries fully into account, further progress will be needed to better understand macro-financial linkages and to sharpen the Fund's ability to identify systemic fragilities and vulnerabilities. Without doubt, proceeding with this endeavor will be essential toward preserving the Fund's role as a trusted advisor to its membership in the context of surveillance, while duly respecting the limits of its own mandate and the responsibilities of other institutions and fora in this area.

IMF Governance

Germany has notified the Fund of its acceptance of the 2010 quota and governance reform well ahead of the deadline. Thus Germany has contributed its share for a timely implementation of the reform and a subsequent strengthening of the Fund's legitimacy and effectiveness.

With regard to the forthcoming review of the quota formula the four principles which underpinned the 2008 reform of the quota formula continue to provide the appropriate basis for the current review: (i) the formula should be simple and transparent; (ii) consistent with the multiple roles of quotas; (iii) produce results that are broadly acceptable to the membership; (iv) and be feasible to implement statistically based on timely, high quality, and widely available data. Furthermore, the formula should be based on verifiable and clear economic criteria and should have a close link to the Fund's mandate that is closely related to countries openness towards the world economy. Against this background, Germany believes that GDP and openness should remain the main elements of the quota formula and considers that openness should carry an increased weight in the formula.

Low Income Countries

Low-income countries (LICs) have become more open and integrated into the global economy. The global financial crisis has had a significant impact on LICs, with many facing a significant deterioration in their external positions. In response to the new situation, the IMF reformed its concessional lending facilities in 2009 to make them more flexible and to meet the increasing demand for financial assistance. The recent review of IMF facilities for low income countries (LIC) showed however that there is room for better tailoring the facilities according to the Fund's mandate and with appropriate conditionality attached. Given the scarcity of PRGT resources Germany supported the use of overall SDR 2.45 billion in

windfall gold sales profits in order to increase the lending capacity of the PRGT to a base envelope of about SDR 1.25 billion in annual average concessional lending capacity. The agreed underlying three pillar strategy is essential to secure the self-sustainability of the PRGT over the long term. Potential modifications to the IMF facilities for low-income countries would need to be designed in a manner that is consistent with this objective.