International Monetary and Financial Committee

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Statement by Mr. Guido Mantega
Minister of Finance, Brazil

On behalf of Brazil, Cabo Verde, Dominican Republic, Ecuador, Guyana, Haiti, Nicaragua, Panama, Suriname, Timor-Leste, Trinidad and Tobago

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The world economy

1. The global economic recovery continues to create a sense of disillusionment. The IMF has probably contributed to that sentiment by what seems to be an entrenched propensity to overstate prospects for advanced economies (AEs), with projections repeatedly contradicted by reality. At the same time, contradictory assessments by the IMF about emerging market economies within a short period also add uncertainty at a time when the world is trying to pull out of the most serious crisis of recent history and initiate a new growth cycle. We urge the IMF to be more realistic in its assessments henceforth.

2. Exceptionally easy monetary policies in the major advanced economies have delivered booming financial asset prices, hence contributing to further income concentration, but their effects on aggregate demand are more modest. Growth in the US picked up momentum after a disappointing first half of 2014, but private investment is sluggish and firms are spending record amounts on buying their own stocks. In Japan, aggressive quantitative easing managed to weaken the yen, but exports barely increased and a sales-tax hike (from 5 to 8 percent) shrank real GDP in the second quarter of 2014 by an annualized 7.1 percent.

3. The euro area is flirting with both stagnation and outright deflation. Current policies have failed to deliver growth and reduce very high unemployment, especially among the young population. Geopolitical tensions between Russia, the US and Europe have contributed to the decline in economic activity and business confidence. The European Central Bank has recently launched new Targeted Long-Term Refinancing Operations and announced purchases of asset-backed securities and covered bonds, as well as its readiness to deploy additional unconventional instruments, should that prove necessary. All these efforts are already weakening the euro. Nevertheless, creating new sources of cheap liquidity and making exports more competitive may not suffice if governments are not given more time to reduce their fiscal deficits.

4. The divergences between cyclical positions and monetary policy trends in the US and the UK, on the one hand, and those of the euro area and Japan, on the other, have

implications for emerging market and developing countries (EMDCs). The main channel for expansionary effects of further monetary accommodation in the euro area and Japan seems to be the exchange rate. This raises the question of whether the US and other AEs would be willing to allow their currencies to further appreciate *vis-à-vis* the euro and the yen. The same question is relevant for EMDCs that have floating exchange rates.

5. EMDCs with dollarized economies or currencies pegged to the US dollar will also be affected. We have a number of such cases in our constituency. A period of prolonged US dollar strength could undermine their competitiveness and external positions – unless their trade is strongly concentrated with the US, which would make the distinction between the effective exchange rate and the bilateral rate with the US dollar of little relevance. The latter is rarely the case. So we can expect this problem to crop up repeatedly if the dollar's strength persists.

6. Financial risks are also impending. Macro-prudential measures could be used to mitigate excessive risk-taking prompted by long-standing accommodative monetary policies in AEs. However, the targeted and specific nature of regulatory and supervisory tools could make them vulnerable to evasive behavior by financial-market participants.

7. The normalization of monetary policy in the US will inevitably lead to higher interest rates and this could result in short-term capital movements with potential adverse effects on financially open EMDCs. But EMDCs are in a relatively stronger position than in earlier periods of financial distress to withstand the tremors from possible capital flow reversals. Though some policy buffers have been drawn upon, international reserves are generally higher – in some cases much higher – and macroeconomic fundamentals including fiscal are generally strong. Reserves of the BRICS economies, for example, stand currently at US$ 5.2 trillion, with China holding US$ 4 trillion, Russia US$ 478 billion, Brazil US$ 373 billion, India US$ 316 billion and South Africa US$ 49 billion as of June 2014. The average gross debt ratio of EMEs and middle income countries is expected to stay just slightly above 40 percent of GDP until the end of the decade, whereas that of AEs is projected to remain above 100 percent of their output levels.

8. EMDCs remain mainly responsible for keeping the world economy afloat*.* This was confirmed by the recent revision of the International Comparison Program for purchasing-power-parity benchmarks. In 2013, EMDCs' total weight in global GDP PPP rose from 51 percent (as derived from the 2005 survey) to 56 percent based on the 2011 survey; conversely, AEs account for only 44 percent of world output. The share of the BRICS in global GDP continued to increase and reached 29.7 percent, surpassing the combined weights of the US (16.6 percent) and the euro area (12.2 percent). China's economy is almost as large as that of the US. The four other BRICS together are larger than the euro area in economic terms.

9. In spite of the slowdown in recent years, EMDCs as a whole are still expanding strongly and real GDP growth is projected to quicken to 5 percent in 2015 – more than double the forecast for AEs. In our own constituency, several countries are posting strong growth rates. The cases of Panama and the Dominican Republic stand out, with growth projected to reach 6.6 and 5.3 percent, respectively, in 2014. In Ecuador, Guyana and Nicaragua growth is also projected to be robust – at or above 4 percent in all three countries.

10. With two out the three major AEs virtually in recession and China's economy expanding at lower rates, some of the commodity exporters in our chair – Brazil, Trinidad & Tobago, Suriname and Timor-Leste – are facing headwinds. Growth in Trinidad & Tobago was affected by a comprehensive maintenance program of the country's energy infrastructure, but is now starting to pick-up and should reach 2.3 percent in 2014. In Suriname, despite lower prices of gold and oil, the economy will continue to expand at healthy rates, between 4 and 5 percent, over the next few years. Timor-Leste, a net oil exporter, has started to successfully diversify its economy and non-oil GDP growth is projected to reach 6.6 percent this year and remain in the 5 to 7 percent range over the medium term.

11. In the case of Brazil, beyond international prices and sluggish demand for exports, economic growth has also been affected by a severe drought. Unemployment has stabilized at record low levels (5 percent in August in the major urban areas) and growth is expected to rebound in 2015 and subsequent years as heavy investment in energy, roads, airports and ports, increase productivity and reduce costs and bottlenecks.

12. Brazil is one of the most solid emerging countries due to, among other factors, a large and dynamic domestic market for consumption, underpinned by a continuous expansion of employment and income; high international reserves; a declining net public debt to GDP ratio; low external indebtedness; and strong foreign direct investment inflows.

13. Recent IMF assessments on Brazil have been contradictory. Some Fund documents attribute the slowdown in growth to internal factors, downplaying the effects of mediocre global economic performance. These assessments contrast with other recent papers published by the institution, such as a study presented in last April's World Economic Outlook that concluded that external factors have been responsible for 60 percent of the growth slowdown in Brazil. Perhaps the IMF needs to consider more carefully its assessments of national economies before publishing them.

14. Low-income countries, as a group, continue to perform strongly. Growth in remains at around 6 percent in 2014 and is expected to accelerate in 2015. Haiti, the only low-income country in our chair, is showing signs of recovery from the devastating 2010 earthquake. In 2013, Haiti's economy grew by 4.3 percent and is expected to grow at a similar rate this year.

Quota and governance reforms

15. By failing so far to ratify the 2010 reforms, the US Congress is preventing the increase and realignment of quotas and voting power within the IMF, as agreed under the 14th General Review of Quotas (GRQ). This undermines the quota-based nature of the institution and its legitimacy and effectiveness.

16. Today, a substantial part of the Fund's resources is no longer available on a permanent and reliable basis. The Fund's lending capacity now largely depends on the New Arrangements to Borrow (NAB), a voluntary mechanism subject to renewal every six months. This situation should not be prolonged. The rest of the membership cannot just sit on its hands and wait whilst the major shareholder remains unable to deliver on its commitments. We need to find alternatives to provide the Fund with permanent and reliable resources and ensure its quota-based nature.

17. Last April, the IMFC agreed in its communiqué that: "If the 2010 reforms are not ratified by year end, we will call on the IMF to build on its existing work and develop options for next steps and we will schedule a discussion of these options". Moreover, the Managing Director stated in the joint session between the IMFC and the G20 that the options for the case of the US not ratifying the 2010 reforms by the end of the year would be ready by early January for discussion with the G20 and the IMFC. We trust the MD's word and fully expect that work on those options is already underway. To prepare for the discussion with the G20 and the IMFC by early January 2015, the Executive Board should meet in advance to examine the available alternatives.

18. As we know, the realignment of quota shares towards EMDCs is the centerpiece of IMF reform. To achieve this goal, the package agreed in 2010 included two forward-looking elements: the comprehensive review of the quota formula and the decision to bring forward the timetable for completion of the 15th GRQ. It was only because of the inclusion of these forward-looking elements that Brazil and other emerging market economies supported the 2010 reforms even with its limited shift of voting power to EMDCs. Thus, as we discuss options to move forward with the 14th GRQ, it is also crucial that we agree on a new quota formula and start working on the 15th GRQ in order to address the increasing mismatch between the relative weights of EMDCs in the world economy and their voice and representation at the Fund.

BRICS Contingent Reserve Arrangement and New Development Bank

19. Last July, Brazil hosted the 6th BRICS Leaders Summit in the city of Fortaleza. On that occasion, agreements were signed establishing the Contingent Reserve Arrangement (CRA) and the New Development Bank (NDB), thus marking the beginning of a new phase of economic cooperation between the BRICS.

20. The NDB, to be headquartered in Shanghai, will mobilize resources for infrastructure and sustainable development projects in BRICS countries and other EMDCs. The NDB will have an initial subscribed capital of US$ 50 billion, equally distributed amongst the BRICS members, and an initial authorized capital of US$ 100 billion. Voting power will be distributed according to the member's subscribed shares. The NDB is expected to start operations in 2016. Membership of the NDB will be open to all other countries.

21. The CRA is a framework for the provision of mutual support through currency swaps in response to actual or potential short-term balance of payments pressures. It will have a positive precautionary effect, helping BRICS countries forestall short-term liquidity pressures while also strengthening the global financial safety net and complementing existing international arrangements.

22. The CRA will have an initial size of US$ 100 billion, with individual commitments of US$ 41 billion from China, US$ 18 billion from Brazil, Russia and India each, and US$ 5 billion from South Africa. Those commitments will only result in disbursements when a country's request to access resources is approved. Access limits will be determined by the countries' commitments times a multiplier. China will have a multiplier of 0.5; Brazil, Russia and India of 1; and South Africa of 2. Each country may request up to 30 percent of its access limit subject only to the CRA's own procedures and safeguards. Above that limit, the existence of an arrangement with the IMF will also be required.

Countries in fragile situations

23. We are pleased to see that the special needs of fragile and conflict-affected states are finally moving up in the Fund's agenda. Last May, a working group of IMF Executive Directors was formed to address their concerns. Under our chair's coordination, it has been promoting joint action on several policy and country items that come to the Executive Board. In February 2015, the Board is expected to start reviewing the Fund's engagement with countries in fragile situation.

24. We have repeatedly called on the Fund to interact more closely with the g7+, the group of 20 countries that constitute the collective voice of fragile and conflict-affected countries. Timor-Leste has played a leading role in the formation and development of the g7+. Haiti is also an active member of the group. For all its initial reluctance, the IMF has by now established a channel with the g7+ through high level meetings at the time of the Spring and Annual Meetings. We appreciate this dialogue and expect it to be translated into concrete actions.

Small developing states

25. The IMF has made some progress, albeit modest, in its agenda for small states. Since the Spring Meetings, the highlight of the work stream on small developing states was the completion of the IMF Staff Guidance Note on engagement with this section of the

membership. Some thematic areas were identified for subsequent investigation – namely: growth and job creation; resilience to shocks; competitiveness; fiscal and debt sustainability; and financial sectors. Some of these issues are relevant to the small states in our chair (Cabo Verde, Guyana, Suriname, Timor-Leste and Trinidad & Tobago). We, therefore, look forward to the faithful application of the guidance note in future bilateral surveillance engagements with small states. The note can also help determine priorities for technical assistance and inform program design. Perhaps more fundamentally, we expect the IMF to be attentive in surveillance of and programs with small developing states so as to ensure high quality results and even-handed treatment.

Climate change

26. The IMF has no particular expertise on the subject of climate change, but heating of the planet could have severe economic implications. Facing this risk requires internationally concerted action and the Fund cannot be absent.

27. IMF members have undertaken different emission reduction commitments. For instance, at the Copenhagen Conference Brazil voluntarily adopted the commitment to reduce by 36-39 percent its projected emissions by 2020. Since 2009 Guyana has a pioneering agreement with Norway to contribute to the struggle against climate change by preserving the rainforest. The commitments that countries adopt inspire national strategies and translate into concrete measures. Beyond helping countries assess and address the fiscal vulnerabilities stemming from the change in climate, the Fund could also offer policy advice to assist the authorities in selecting and designing measures better adapted to the countries' objectives and circumstances.