Statement by Mr. Guido Mantega
Minister of Finance of Brazil

On behalf of Brazil, Colombia, Dominican Republic, Ecuador, Guyana, Haiti, Panama, Suriname, Trinidad and Tobago
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International Monetary and Financial Committee

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The World Economy and Financial Markets

Since we last met in October, the economic crisis has spread to practically all countries. Most developing nations are now experiencing a severe growth slowdown with increasing unemployment and underemployment. Among the larger emerging market countries, China, India and Brazil still have relatively favorable economic indicators in 2009, albeit less favorable than in previous years.

In the developed world, the outlook is even worse. GDP will contract sharply. For 2009, the IMF is projecting a decline in GDP in 32 of the 33 advanced economies. The sole exception is Cyprus that is expected to have zero growth.

Notwithstanding these dismal projections, it is fair to say that we have recently been seeing the first, still tentative, signs of improvement. Financial markets seem to be less nervous. The financial systems in the United States and in large parts of Europe are still very fragile, but even in this area there are indications that a recovery may have begun.

Part of this improvement is probably due to the large-scale efforts that governments and central banks are undertaking, especially since the end of last year, to counteract recessionary forces. However, in some countries, anti-crisis measures still fall short of what is required. Moreover, not all measures that were announced since October have been implemented. We need to move faster from announcements to actions in order to restore confidence and restart growth, through both conventional and unconventional means. This is particularly true in the financial sphere. Lack of decisive action may lead to a protracted recession. We welcome the IMF’s recognition that some countries may have to resort more extensively to temporary nationalization of financial institutions if the crisis is to be overcome.

Our main goals should be to restore the supply of credit, support international trade and sustain capital flows. If we fail in this, restructuring of debt will become unavoidable, with lasting damage to confidence and economic recovery.
The Role of the G-20

Devastating as it is, the ongoing crisis has given new impetus to policy coordination on economic and financial issues. Countries seem to realize that joint action is more effective and that “beggar-thy-neighbor” policies have to be avoided if we are to escape a repeat of the 1930s.

The G-20 is the most significant example of policy coordination. Since the last IMFC meeting in October, the group has met twice at the level of heads of states and governments and will meet again this year, in September, in New York. The G-20 has launched unprecedented actions to promote economic recovery and financial reform.

We must not lose political momentum. Part of the recent improvement in market sentiment can be attributed to the outcome of the G-20 Leaders’ Summit in London. In this regard, the commitment to boost the IMF’s resources seems to have had a considerable effect on financial indicators and market behavior.

Unlike other such groupings, in the G-20 developing countries are represented. This allows for a division of protagonism and responsibilities. The G-20 is a consensus-based mechanism in which the views of developing countries can be given adequate consideration. Since the end of last year, it has become the focal point for economic policy coordination at the international level and we believe that it will continue to play this role.

The G-20 working groups, including the Working Group on the IMF, contributed significantly to the preparation of the London Summit. However, these working groups have not concluded their work program and must follow-up on the decisions taken in London and on the medium-term objectives established in the G-20 Washington Summit last November. As we prepare for the New York Summit, we should make sure that these working groups continue to discuss the international economic and financial agenda and prepare specific policy recommendations.

Needless to say, policy coordination mechanisms, like the G-20, do not replace international financial institutions or make the need to strengthen them less urgent. On the contrary, the G-20 has recognized the IMF as a key pillar for addressing the current crisis and preventing future ones.

We believe that strengthening the IMF requires work on three fronts: i) increasing resources; ii) reforming lending instruments and conditionality; and iii) fixing the democratic deficit.
Increasing IMF resources

One of the most important results of the G-20 London Summit was the agreement that IMF resources should be increased by US$ 500 billion relative to pre-crisis levels. As we move towards this goal, some principles should serve as the basis for our actions.

First, immediate and near term borrowing arrangements should have a temporary nature and serve as a bridge to a permanent increase of resources through a general quota review. The Fund is a quota-based institution and borrowing arrangements should be designed in a way that does not undermine the next general quota review to be concluded – as agreed by the G-20 – by January 2011. Depending on how they are designed, IMF notes or bonds could be an option to provide immediate resources to the institution without undermining the reform process. The New Arrangements to Borrow (NAB) may not constitute an adequate mechanism because it is a standing arrangement. Its expansion could limit the scope for and delay quota reform. We could support a proposal to set up a provisional plurilateral agreement, a Temporary Arrangement to Borrow (TAB), with more flexible rules than the NAB.

The second principle should be that the size of contributions from member countries reflect their respective obligations and rights in the Fund. IMF quotas could serve as a benchmark for establishing the size of contributions from countries that are in a position and willing to make them.

Third, the design of financing instruments should allow the treatment of members’ contributions as international reserves. Thus, contributions should involve the acquisition of liquid assets issued by the Fund that could be immediately converted into freely usable currencies, if the need arises. This aspect is particularly important for countries that do not issue reserve currencies.

Fourth, countries may wish to split their contributions in two parts, as is being done by the European Union. A part of the contribution could be reserved for bilateral/regional support in addressing balance-of-payments crises, inter alia through the co-financing of IMF programs. Contributions would thus better reflect countries’ economic and regional priorities.

Lastly, countries may also wish to allocate part of their contribution to the financing of the poorest countries. Brazil will look into ways to contribute to enhancing the Fund’s lending capacity for low-income countries.
Reforming the IMF’s Lending Instruments and Conditionality

Financial resources will be of no avail if they are not accessible through appropriate instruments. In the past, low access levels and excessive and intrusive conditionality have prevented the Fund from being helpful to countries that needed its support. For many years, developing countries have asked for the streamlining of conditionality, but faced resistance from the advanced countries. The current crisis, however, has significantly changed this perspective. Governments and central banks of developed countries were led to resort domestically to remedies that they were reluctant to allow the IMF to adopt. They learned by harsh experience the value of rapid provision of liquidity and high access to resources with few conditions.

Since last year’s Spring Meetings, our chair has systematically argued in favor of providing the Fund with an entirely new instrument capable of quickly providing liquidity to countries hit by financial turbulence and external shocks. We presented a specific proposal for such a new liquidity instrument directed at countries with sound economic policies and integrated in international financial markets. After an unsuccessful first step last October with the Short-Term Liquidity Facility, which was never used, further discussions led to the creation of the Flexible Credit Line (FCL) in March. This instrument provides large upfront support with no conditionality. Access to the FCL is quick and almost automatic. Only countries with a strong track record of sound economic policies qualify for this facility.

The recently approved changes in the Fund’s lending framework and the establishment of the FCL represent a radical departure from past practices. In a matter of less than one month, three countries (Mexico, Poland, and Colombia) have requested access under the FCL. Mexico’s request has already been approved by the Executive Board. Poland’s and Colombia’s requests are under consideration by the Board and are expected to be approved shortly.

We also welcome the decision to double access limits on concessional lending by the IMF to low income countries under the Poverty Reduction and Growth Facility (PRGF) and the Exogenous Shocks Facility (ESF). We look forward to the planned reform of the IMF’s lending framework for low-income countries.

As the financial landscape evolves, it is important that we monitor closely the implementation of all modifications introduced in the lending instruments and remain open to make further innovations and adjustments if needed.

In our attempt to build a more stable financial environment, it is important to reflect on the role of the IMF in the international monetary system in light of the lessons of the crisis, including with respect to major reserve currencies. Increasing the role of the Special Drawing Rights (SDR), a multilateral reserve asset issued by the Fund, is one way of achieving a more balanced international monetary system, less dependent on a few national or regional currencies. For this reason we proposed at the G-20 London Summit a new general allocation of US$ 250 billion and expect the IMF to move expeditiously to put this into practice. We will support the development of proposals to effect a second-round
distribution of SDRs to developing countries. Under the current skewed distribution of quotas, about 60 percent of the new allocation will go to developed countries. We also hope that further SDR allocations will occur in the future, so as to make the provision of international liquidity gradually less dependent on the monetary policies of the few countries that issue reserve currencies.

**Fixing the Democratic Deficit**

Crisis is an appropriate time for learning what we did wrong and trying to avoid repeating the same mistakes. The IMF repented from many of its past sins. But it still has to address the original sin: its democratic deficit. We value the Managing Director’s efforts to build a modern IMF, with an appropriate set of instruments and policies. However, we expect political willingness to move faster in the direction of greater representation of developing countries in this institution.

The governance reform agenda should remain firmly focused on quota review. A significant quota realignment should be completed no later than January 2011 in order to better reflect the economic weight of member countries and to increase the quota and voting shares of developing countries. The Fund’s legitimacy depends on this.

The selection of the heads of the IMF and the World Bank should be through an open, merit-based process, abandoning the practice of allocating these positions exclusively to European and American nationals. This practice dates back to the creation of the Bretton Woods system and has no place in the 21st century. We realize of course that it will be difficult to achieve this without substantial quota realignment.

Other issues have been raised in the reform discussions, some of which relate to the IMFC. We believe there is room for strengthening of the IMFC and we would like to make some proposals. First, the draft communiqué should be submitted to us with sufficient anticipation to allow better preparation and more involvement of Governors in its discussion, as already done in the Development Committee. Second, our plenary sessions could be less formalistic and more interactive, with more room for Governors to express their points of view. Third, we should avoid the practice of bringing up issues at the last moment, forcing Governors to take hasty and on the spot decisions about topics about which no preparatory discussions have taken place. We believe that the strengthening of the IMFC, that functions as a consensus mechanism, is the appropriate way of deepening the engagement of Governors in the IMF’s work.

We believe that the proposed activation of a ministerial-level Council, recently resuscitated by some countries, adds nothing to our involvement in IMF affairs. We, Governors and Ministers, already make the major decisions ourselves – either directly (when we vote on the most important issues in the Board of Governors) or through our representatives in the Executive Board.
If activated the Council would replace the IMFC, but with a fundamental difference: the Council’s decision-making rule, as contained in the Articles of Agreement, is the same that applies to the Executive Board. With the voting shares that prevail in the Fund at present, the Council is a much more unattractive body for most of us than the present consensus-based IMFC. The only way this could be remedied would be through a substantial reform of quota and voice. Otherwise, the activation of the Council would be a counter-reform, since developing countries would lose influence in the IMF. Moreover, the Council may also weaken the G-20, another consensus-based body in which developing countries are represented.

Finally, the IMF takes pride in its universal membership, and rightly so. However, this can be improved, correcting an omission that has lasted a long time. I am referring of course to Cuba, the only country in the Western Hemisphere that is not a member of this institution. The time has come to open our doors to Cuba.

Thank you.