**International Monetary and Financial Committee**

Twenty-First Meeting
April 24, 2010

**Statement by Mr. Guy Quaden**
**Governor of the National Bank of Belgium**

**On behalf of Austria, Belarus, Belgium, Czech Republic, Hungary, Kazakhstan, Luxembourg, Slovakia, Slovenia and Turkey**

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**Governor of the National Bank of Belgium**
**On behalf of**
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**At the 21st International Monetary and Financial Committee**
**Washington DC, April 24, 2010**

## The Global Economy and Financial Markets

A more sustained recovery worldwide is supported by renewed strong growth in emerging countries in Asia and elsewhere. Output growth in the US is projected to be above potential already this year. The Euro area and other countries in the European Union have also overcome last year's deep recession and may reach their potential growth rates in 2011. However, in a few countries with deep seated problems which pursue vigorous policies to restore external competitiveness and fiscal soundness, the recovery will occur at a later stage.

The multispeed recovery in the world economy requires policy actions that are specific for each country and region. Our Committee must ensure that these policies are mutually coherent and supportive.

While most recent developments are encouraging, the legacies of the severe recession are significant and long lasting. They heighten risks of renewed crises and require determined well sequenced and closely coordinated policy actions.

In advanced countries, with policy interest rates close to zero and fiscal deficits and public debt elevated, the room for policy action is small, if not exhausted, in the event that the recovery falters. Therefore, it is wise counsel of the IMF that monetary and fiscal policy should remain supportive this year, except in countries facing more urgency to start fiscal correction, or in those emerging markets with signs of overheating.

In the European Union, governments have agreed on ambitious timetables to reduce fiscal deficits below 3 percent of GDP and on the pace to reach fiscal balance, thereby steadily reducing debt-to-GDP levels. If combined with the design and communication of credible medium-term specific consolidation measures, this strategy will preserve and strengthen market confidence and assure continued low funding costs.

Fiscal consolidation should be designed to increase the economy's potential growth by lowering labor income taxation, higher consumption taxes and lowering government spending and transfers.

Employment destruction is a very significant cost of the crisis. Even if we are observing the first signs of renewed modest job creation, the unemployment rate may remain elevated for some time. Government and social partners should adhere to internationally agreed principles to support employment creation with high quality education, job training and labor market policies that set the right incentives. We encourage the Fund to closely cooperate with the International Labor Organization (ILO).

Emerging markets where the recovery is most advanced will have to start or continue raising interest rates to contain inflationary pressures and lower tensions in asset markets.

As capital flows to these countries increase, monetary tightening should be supported with nominal exchange rate appreciation, fiscal tightening, macroprudential measures, easing of controls on capital outflows and some buildup of reserves. Controls on capital inflows should be temporary and designed to avoid distortions. Countries that promote better resource allocation and higher value added industries will help offset the contractionary effects of real exchange rate appreciation.

To reduce global imbalances, countries with excessive deficits must encourage private savings, reduce public deficits and more generally improve external competitiveness. Countries with excessive surpluses must encourage domestic demand, inter alia by establishing adequate social security systems, and allow exchange rate appreciation.

Major parts of the financial system are now on a more stable footing. Policies should help address the remaining problems of shortage of capital, asset deterioration, weak profitability, and short funding maturities that may constrain the financial sector's capacity to support the recovery.

The pace of unwinding the exceptional support measures for the financial sector and the pace of introducing new capital adequacy and liquidity management requirements should be decided to ensure both support to the recovery and steady progress with financial sector repair.

The Spanish Minister, Ms. Elena Salgado, has provided a good summary of the significant progress made with reforming prudential regulation and supervision of the financial sector in the European Union.

Our experts who work on the technical aspects of the overhaul of the regulatory and supervisory system will greatly benefit from the research and proposals formulated by the staff of the IMF on how best to contain systemic risk in the financial sector, how to reduce the risk in the uncontrolled OTC derivatives market, how to assess interconnectedness as a source of systemic risks and how taxation of financial institutions could create incentives for less leverage and less risk taking.

We are also considering establishing an integrated crisis management and resolution framework for the EU's single market that could deal cost effectively with failing systemic cross-border banks. Here again, we acknowledge the useful contributions by the Fund experts to our work.

We should aim for the completion of this important work by the end of this year. This would bring about much needed clarity for the financial sector. The new regulatory framework would increase to some extent the cost of intermediation. At the same time, it should significantly enhance stability in the global economy. In terms of long-term sustained growth, its outcome will be clearly positive.

**The IMF's Crisis Response and Reform Agenda**

*Fund surveillance*

The crisis has demonstrated that we need to collaborate better and that Fund surveillance must improve at the level of individual countries, regions and the global economy.

With the explosive growth of international capital flows largely intermediated by the financial sector, surveillance should focus more on cross-border capital flows, macrofinancial stability and spillover effects between the real and financial sectors, national and international. Assessing the stability of the financial sector is critical and should be an integral part of Fund surveillance.

Surveillance at the country level remains central but it no longer suffices.

Assessing international coherence and promoting coordination among national policies should remain a central objective of our collaboration. It must be pursued with close involvement of high level authorities.

Over the past years the Fund has developed high quality analysis of developments and policy challenges in both the global and regional economies and financial markets. These have recently been complemented with the Early Warning Exercise. The staff proposes yet an additional new report on international spillover effects. All these activities and reports of multilateral surveillance could be streamlined and better integrated. Their analytical content remains a critical background. Proposals to produce once a year a more focused, policy oriented, multilateral surveillance report could be considered. It goes without saying that in such a report attention should be paid to how economic developments and policies in one country affect other countries and to unsustainable imbalances and developments in the global economy, as well as to the underlying causes. Its purpose should be to foster collective policy actions in response to the identified common vulnerabilities. Discussing the multilateral surveillance report and agreeing on the needed policy actions could become a central mandate of our Committee.

In all this, the Fund should closely collaborate with the FSB and the standard setting bodies.

*Fund lending*

Fund lending should promote a stable financial position. Under such circumstances, Fund lending enhances policy credibility. It helps to preserve or regain financial market access and provides remedy for market failure. Fund lending should facilitate the proper functioning of the markets and their signaling effects.

Countries should ask Fund financial assistance in a timely manner. Precautionary credit lines help safeguard financial stability and should be encouraged. Last year's launching of the flexible credit line and the high access precautionary stand-by arrangement was a right step towards strengthening of the Fund's lending instrumentarium. The Board should continue to consider how Fund lending could contribute to a more stable international financial system.

Creating different lending instruments to signal different levels of policy strength is a potential source of friction when a country is not –or no longer-eligible for a specific instrument. It may discourage countries to ask the Fund credit as this will be perceived as a signal of weakened economic position. We continue to favor one single flexible (precautionary) credit line that gives access according to the merits and the strengths of each individual case.

*Fund resources*

The amount of Fund credit should be relevant for helping countries with large (potential) balance-of-payments needs, but limited to the country's repayment capacity and to avoid overstretching the Fund's limited resources and moral hazard.

The size of international capital flows and the worldwide transmission of shocks within the global financial system necessitate a sizeable increase of the Fund's lending resources.

Six countries in our constituency (Austria, Belgium, the Czech Republic, Luxembourg, the Slovak Republic and Slovenia) are committed to provide bilateral loans to the Fund to bolster the Fund's lending capacity. In the medium term these bilateral loans should be replaced by the expanded and enlarged NAB . Loan agreements with Belgium, the Czech Republic, and the Slovak Republic have already been concluded.

The approval of the enlarged and expanded NAB is most welcome. We call for its swift ratification and implementation.

The NAB complements quota resources. It cannot substitute a substantial quota increase necessary to support the Fund's long-term ability to meet member countries' balance of payment financing needs. The size of the NAB should be reviewed when agreement on the quota increase is reached.

*The Fund's role in low-income countries*

The global financial crisis has hit low-income countries. Sound macroeconomic policies and reforms to elevate human resources, and promote investment and employment, help to reduce poverty and achieve high sustainable growth. The Fund's role in promoting such policies remains critical.

The simplified concessional lending framework for low-income countries came into effect last January, with the consent of all lenders and contributors to the Poverty Reduction and Growth Trust (PRGT). This was a welcome achievement. It must now be followed up with the provision of adequate resources to the Trust. The lending capacity of the PRGT must be augmented urgently. We welcome the commitments made in this respect by several countries.

*Fund governance reform*

Countries that have not yet ratified the quota and voice reform agreed in April 2008 should do so as soon as possible.

The fourteenth general quota review should result in a significant increase, if not a doubling of quota. Underrepresented countries, most of them being emerging market and transition economies, should see their actual quota share increase, in accordance with the existing quota formula and the Pittsburg/Istanbul agreements. The realignment should ensure that no country is more underrepresented after the reform than it was before and that no over-represented country becomes underrepresented. The voting power of the group of the poorest countries should be protected.

The current size of the Executive Board strikes the right balance between effectiveness and inclusive representation. Developments in quota shares, through the election of Executive Directors, will be reflected in the Board composition.

We support a merit-based selection of senior management without geographical preferences, and a balanced distribution of IMF staff in terms of geographical origin as well as professional and academic background.