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Statement by Elena Salgado
EU Council of Economic and Finance Ministers

Statement by Minister of Finance Elena SALGADO,
in her capacity as Chairwoman of the EU Council of Economic and Finance Ministers, at the IMFC Spring Meeting, Washington, D.C., April 24, 2010

1. I submit, in my capacity as Chairwoman of the EU Council of Economic and Finance Ministers, this statement which focuses notably on the world economy, in particular the outlook and policies for the EU, and on IMF policy issues.

2. In view of current challenges, the euro area Member States on 25 March reaffirmed their willingness to take determined and coordinated action, if needed, to safeguard financial stability in the euro area as a whole and outlined the mechanism for such an action. While the EU framework for budgetary surveillance has generally led to results which compare well at a global scale, the most recent developments demonstrate the need to strengthen and complement the existing framework to ensure fiscal sustainability in the euro zone and enhance its capacity to act in times of crises. For the future, surveillance of economic and budgetary risks and the instruments for their prevention, including the excessive deficit procedure, must be strengthened. Moreover, a robust framework for crisis resolution, respecting the principle of Member States' own budgetary responsibility, is needed. Therefore, the Heads of State or Government of the EU have agreed at their meeting on 25-26 March 2010 to install a task force to present to the Council, before the end of this year, the measures needed to reach this aim, exploring all options to reinforce the legal framework.

Economic Situation and Outlook

3. The global economy has started to recover, though the strength of the recovery is uneven and the stimulus measures introduced during the crisis still play an important role. The recovery has been led by strong growth in several emerging markets, particularly in Asia. Indicators of global trade, industrial production as well as business and consumer confidence during the last few months have been encouraging. However, labour market and fiscal developments in some countries are a concern. Conditions in the financial markets have improved but remain fragile. The situation in the interbank market has not fully returned to normal. Bank lending to the private sector and securitisation remain relatively low, and small and high-yield non-financial enterprises still struggle to access external finance. Further out, the global recovery is expected to be uneven and surrounded by uncertainties. The global economy could experience another soft patch once fiscal and monetary stimuli will be phased out, and private demand will have to play a more prominent role. Priority should be given to mitigating the negative consequences of the recession (notably the high levels of unemployment and the loss in potential output in many countries) in an appropriately co-ordinated way among governments, together with implementing sustainable growth strategies for the future that will enhance the growth potential of our economies.

4. In the EU, the exceptional measures put in place have been playing a key role and the EU economy has been gradually recovering, whilst still facing headwinds. Both upside and downside risks appear to have recently intensified. While there are some grounds for optimism, mainly due

to a better-than-expected external environment, investment fundamentals remain weak and the labour market performance poor. Preventing persistently high unemployment levels should be one of our priorities in the coming years. The overall situation in financial markets has improved but remains weak, and recent nervousness in equity and debt markets has confirmed that downside risks remain. EU banks have continued to repair their balance sheets on the back of improved earnings and more favourable funding conditions. However, bank refinancing conditions have not fully normalised, in particular as regards the availability of medium to long-term financing.

Policy Developments

a) Macroeconomic and structural policies

5. First steps have been made to start exiting from the fiscal and monetary stimulus as well as from financial sector support. We should agree on the principles of an ambitious, comprehensive and coordinated exit strategy from fiscal stimulus and financial support measures to anchor expectations and reinforce confidence, as an important component of ensuring a sustained economic recovery. The strategy needs to be fully implemented as the recovery becomes self-sustained. Cooperation between governments should help to ensure a proper timing and sequencing of exit, taking each region's circumstances into account. The strategy should be consistent with regional fiscal policy agreements, notably European commitments under the fiscal rules of the Stability and Growth Pact. The IMF should contribute to this process, reviewing individual exit policies and implementation, and assess their collective impact on the global economy and financial system. Provided that the recovery is strengthening and self-sustaining, the fiscal stimulus in EU countries should be phased out by the end of 2010 and fiscal consolidation in all EU Member States should start in 2011 at the latest as agreed by the Ministers of Finance in order to halt and eventually reverse the increase in debt and restore sound fiscal positions. Maintaining the current fiscal expansion for too long would lead to further unsustainable debt trends, which could weigh on the growth capacity of the economies going forward, adding to the already daunting challenge of ageing. Overall, fiscal consolidation must be ambitious. However, the speed of consolidation should differ across Member States, depending on the individual economic situation, fiscal challenges and macro-financial risks. Moreover, flanking policies should be encouraged, such as strengthened national budgetary frameworks or reform of age-related entitlements, and structural reform efforts should be deployed to raise potential growth.

6. A timely and credible exit strategy for fiscal policy is also important to improve the prospects for price stability. The European Central Bank has announced the first steps to exit from the non-standard measures, which will gradually lead to the re-absorption of the ample liquidity provided during the crisis and a normalisation of the ECB's operational framework. Progress with financial repair is essential to ensure that the banking system makes its best contribution to the recovery process and is well equipped for the normalisation of central bank liquidity. Reforms of financial regulation and supervision should be continued and appropriately coordinated also at the global level.

7. The EU will set out its Europe 2020 strategy for jobs and growth. The new strategy will focus on the key areas where action is needed: knowledge and innovation, a more sustainable

economy, high employment and social inclusion. The strategy will be comprehensive, involving a broad range of policies addressing Europe's major short-term macroeconomic challenges and long-term challenges regarding potential output. The strategy will be coordinated at the EU level to ensure that synergies are exploited. It will ensure that policies reach their objectives in the most cost-effective way and maximise synergies.

8. Overall economic policy coordination will be strengthened by making better use of the instruments provided by Article 121 of the Treaty (TFEU) and coordination at the level of the euro area will be strengthened in order to address the challenges the euro area is facing. The timing of the reporting and assessment of the different programmes should be better aligned, in order to enhance the overall consistency of policy advice to Member States. The integrity of the Stability and Growth Pact will be fully preserved.

9. Global imbalances remain a challenge for global macroeconomic and financial stability. Without an appropriate multilateral strategy to structurally reduce those imbalances, the strength and sustainability of the recovery may be negatively affected. The new Framework for growth agreed by the G20 Leaders in Pittsburgh provides a welcome opportunity for strengthening cooperation and promoting the adoption of sound policies among major economies in order to achieve more balanced global growth and avoid the re-emergence of global imbalances. It is important to make progress on the framework so that it optimally supports a constructive dialogue on tackling those imbalances. The institutional and economic policy set-up of the EU and the euro area should be fully taken into account in that respect. This implies that in its analysis, data work, and reporting in the context of the G20 assessment process, the IMF should refer to EU and euro area aggregates where appropriate, in particular when referring to common policy-making, notably monetary and exchange rate aspects, the relevant structural reform frameworks, the Stability and Growth Pact, and to the current account balance.

10. The EU calls on its partners to refrain from protectionist measures and to promote a stable and well functioning international monetary framework. Reserve accumulation of recent years may in particular provide emerging economies with a precautionary buffer but an excessive build-up of reserves creates undesirable distortions for both the domestic and the global economy, in the form of exchange rate misalignments and contributions to the accumulation of global macroeconomic imbalances. The EU supports the ongoing work to assess the experience with the revamped multilateral lending instruments during the financial crisis, as well as the need to assess the implications of a broader range of financial safety nets available to countries to respond to macroeconomic shocks.

b) Financial market policies – state of play of regulatory reforms

11. The EU has made significant progress during recent months in developing a more efficient regulatory and supervisory architecture. 2010 is a crucial year for implementing the agreed financial reforms commitments and to continue to deliver on future reforms. We believe that as to future regulatory reforms, work on the following proposals/issues should continue:

12. The implementation of Basel II at an international level is of key importance. At the same time, the capital framework must be developed further to ensure that banks hold an adequate level of capital to withstand and absorb losses and that the quality of capital is further improved. The

EU has implemented Basel II and is working in parallel with the Basel process to enhance the current framework for capital and liquidity. It is essential that such an enhanced framework will be implemented at a global level. The EU is also participating actively in the debate regarding systemically important financial institutions, which should be treated in a consistent and globally coordinated way.

13. Derivative markets should be subject to greater transparency and produce less counterparty risk. Transparency shall be increased by promoting centralised trading and by mandatory reporting of non-centralised trades to Trade Repositories, that should themselves be subject to adequate supervision, and to which micro- and macro-prudential supervisors and central banks should have timely and unfettered access. Concerning counterparty risk, there is an urgent need for clearing eligible derivatives through well capitalized and well managed central counterparties subject to effective regulation, and supervised with high and harmonised prudential and operational standards. To enhance the resilience of the OTC derivatives market the European Commission will present a legislative initiative in June 2010.

14. A new financial supervisory framework in the EU should be in place in early 2011. This framework will be based on the European Systemic Risk Board which will monitor and assess risks and threats to the stability of the financial system as a whole (macro-prudential supervision) and the European System of Financial Supervisors, comprising European supervisory authorities for banking, insurance and securities (micro-prudential supervision) with binding regulatory and supervisory powers.

15. Hedge funds and private equity activities have come under increasingly sharp international scrutiny. Regulatory initiatives on alternative investment funds and managers should be based on the assessment of systemic risks, the need to preserve market integrity, efficiency and transparency towards counterparties and investors, as well as investor protection. Future registration of funds and their managers is a focal point. At the EU level, the Directive for Alternative Investment Fund Managers (AIFMD) is currently under negotiation and is expected to be adopted in summer.

16. The EU is working on a new framework for crisis management. We are particularly concerned about the need to safeguard the internal market and underpin it with effective crisis management arrangements which allow banking crises to be more effectively handled across borders.

17. The EU has already adopted a regulation which will subject credit rating agencies to mandatory registration and supervision in order to ensure the integrity of the rating process, the new European securities and markets authority being responsible of these competences from its creation early 2011 onward.

18. Accounting standards are another key area. The EU has called upon accounting standard setters to work in order to achieve a single set of high quality, global standards. While maintaining transparency for investors, accounting standards should not aggravate pro-cyclicality of financial markets and should not undermine the implementation of prudential rules. Standard setters should refer to the BCBS principles for the revision of accounting standards for financial instruments issued by the Basel Committee in August 2009.

19. The work on non-transparent and non-cooperative jurisdictions, including off-shore centres, needs to continue in order to achieve compliance with the OECD-standard on exchange of tax information, improve their standards to fight money laundering and terrorist financing and enhance their effective compliance with prudential regulatory and supervisory standards, in particular on cross-border cooperation and exchange of information.

20. Implementation of international rules adopted with respect to compensation practices in the financial sector should be pursued, in a consistent manner.

c) Contributing to a more favourable international environment

21. Markets should be kept open and all forms of economic protectionism avoided. Implementing the commitments not to impose new trade and investment restrictions and not to create new subsidies to exports is essential. There is a need to re-affirm that it is in our mutual interest to support trade by promoting the orderly supply of trade financing, and to avoid competitive devaluations and anticompetitive measures. On international trade policy, we need to deliver on the commitment to reaching an ambitious, comprehensive and balanced conclusion of the Doha Development Round in 2010. Progress so far has been disappointing. Concluding the Doha Development Round in 2010 will require an important acceleration in the negotiations. We should underline our readiness to deliver on this objective, on the basis of the progress to date. We should also reaffirm our rejection of protectionist measures ("standstill commitment").

IMF Policy Issues

22. EU Member States welcome the efforts undertaken by the IMF to address the challenges generated by the current financial crisis and the decisions taken over the last months to adjust its instruments and financial set-up to ensure that it can assist members effectively in the current global economic and financial environment. We recognise that further reforms regarding the IMF's mandate, scope and governance is warranted to strengthen the IMF so that it better meets the needs of its membership and fully addresses the challenges posed to the global economy in the 21st century. EU members will continue to contribute constructively in this process.

IMF resources

23. EU Member States call for a swift implementation of an expanded and more flexible NAB to facilitate the IMF's continued efforts to address financial needs in order to forestall or cope with an impairment of the international monetary system. In this context, all EU Member States who are eligible for NAB-membership are ready to provide their share of USD175bn to the NAB. Regarding SDR voluntary arrangements, many EU countries are participating and we encourage other countries to do the same to help guaranteeing the liquidity of the SDR.

24. EU Member States will continue to contribute to the resolution of the current crisis through the Community's Medium-Term Financial Assistance Facility. We appreciate the close cooperation between the IMF and the EU in designing programmes.

IMF reform – quota and broader governance

25. EU Member States fully share the view that modernizing IMF governance is essential for improving the Fund's credibility, legitimacy, and effectiveness in the post-crisis environment. The review of the Fund's governance should be comprehensive and address the full range of quota as well as non-quota reform elements as agreed in Pittsburgh and Istanbul. EU Member States insist that the reforms should be delivered together as a single package and within the same time frame. We also reiterate that the governance reform process should be fully anchored within the relevant IMF bodies, and should engage all members of the IMF.

26. The overall size of quotas should primarily reflect the IMF's long-term ability to meet member countries' balance of payment financing needs. The nature of the IMF as a quota-based institution should be preserved. Consequently, an increase in the overall size of quotas should be accompanied, as agreed, by a comprehensive review of the NAB and/or bilateral resources to ensure an appropriate overall size and balance between quota and borrowed IMF resources, so that the NAB will continue to play its role as a back-stop to quota resources.

27. EU Member States remain committed to the goal of aligning members' quotas and voice to better reflect their relative weights in the world economy and their capacity to support the Fund's work, with all countries taking their fair share in the financing burden. The current quota review should achieve a shift of above, but close to 5% of quota shares from over- to underrepresented countries. This shift will benefit predominantly underrepresented emerging and developing countries but underrepresented advanced countries should be treated equally. Overrepresented countries, both advanced and emerging market economies, should make a contribution to the shift. At the same time, voting shares of PRGT-eligible Low Income Countries (LICs) in the IMF should be protected. The realignment of quota should be principle based so that it affords equal treatment to all IMF members. We do not see merit in re-opening the quota formula which should serve as the sole basis to determine whether a country is over- or underrepresented. On the contrary, it would dramatically endanger our capacity to conclude the quota review by end January 2011. The main objective of the quota review should be to reduce the degree to which countries are out of line with their calculated quota shares. The review should ensure that no country is more underrepresented after the reform than it was before and that no over-represented country becomes underrepresented. EU Member States are ready to contribute in achieving these objectives.

28. EU Member States share the view that a greater ministerial engagement in providing strategic direction to the Fund and increasing its accountability is essential to the institution's effectiveness. The Fund would benefit from a greater political traction and ownership by its members. A strengthening of the IMFC, including by having more interactive IMFC meetings and introducing an alternative Troika leadership model, merit further consideration, but the fundamental debate on the competences and authority of the IMFC is also needed. We support a clearer delineation of responsibilities between Governors and Ministers, the Executive Board and IMF management, as well as increasing accountability of the Executive Board and management, and believe this should form part of the current discussion on IMF governance reform.

29. EU Member States do not support a reduction of the size of the IMF's Executive Board as the current size reasonably well strikes the right balance between inclusiveness/legitimacy and an

effective functioning of the Fund. We support further discussions on ways to enhance the Executive Board's effectiveness, including by streamlining procedures. We believe it is premature at this stage to discuss moving to an all-elected Board.

30. EU Member States propose considering in more detail the lowering of the thresholds required for special voting majorities. This could contribute to a more inclusive decision making process. We also welcome further work on Double-majority voting on a limited range of issues, provided it does not undermine the IMF's decision-making capacity.

31. EU Member States welcome the increasing diversity of IMF management and staff and encourage the institution to make additional progress and to report on this issue during the Annual Meetings. We restate that a balanced distribution of IMF staff is desirable, in terms of geographical origin as well as professional and academic background.

32. Heads and senior leadership of all international institutions should be appointed through an open, transparent and merit-based process, irrespective of nationality and gender. The criteria and the procedure for the selection process of the IMF Managing Director should be part of a broader reform including top management from other international financial institutions including in particular the World Bank.

IMF mandate – surveillance and lending framework

33. With the fading out of the worst of the crisis we have a good opportunity to discuss further the future role of the Fund, including the functions of the IMF as well as possible improvements to the surveillance framework and the IMF's crisis resolution and prevention tools.

34. The IMF's primary role should be crisis prevention by offering high quality surveillance, policy advice and warnings to the country concerned and to the international community. This is crucial to contribute to the proper functioning of the global economy. Bilateral surveillance should continue to be one of the main stays of the IMF's surveillance, and its traction on members' policies should increase with a view to strengthening the IMF's crisis prevention role. EU Member States also strongly support a deepening and strengthening of the multilateral and regional aspects of surveillance. In that context, we urge the IMF to make full use of its comparative advantage to increase its focus on cross-country spillover effects.

35. EU Member States welcome a clarification of the IMF's mandate in relation to the financial sector. We support making Financial Sector Assessment Programs and regular updates mandatory for all countries with *systemic* importance. The implications of conferring to the Fund a clear oversight on the capital account as an alternative to a mere advisory role on capital flows and related policies should be further explored.

36. Crisis resolution and prevention through financing is also an important and an integral part of the IMF's work. Indeed, the recent crisis has demonstrated the importance of effective crisis prevention, including through the use of precautionary lending instruments. We see merit in reflecting on the IMF's toolkit, assessing the experience with both the traditional and the revamped lending instruments during the financial crisis, and considering as well financing implications of possible changes.

37. EU Member States underline that the Fund's lending is only one element of a potential "financial safety net" at the global level, which would imply making full use of the synergies between existing instruments such as reserve accumulation, swap arrangements among major central banks, and other regional arrangements. The IMF can play an important role in making bilateral, regional and multilateral arrangements work together. We would welcome further work by the Fund on the broader range of tools available to countries to respond to macro shocks and which may provide efficient complements to existing financial safety nets.

Role of the IMF in low-income countries (LICs)

38. Low-income countries (LICs) are still under great strains and international support is required to help them address the impact of the crises. The IMF has been at the forefront in supporting them, making available loan resources under the PRGT fall to near record lows. In this respect, we welcome the establishment of a new framework for mobilizing concessional loan resources that seeks to meet the various needs and preferences of different creditors. We believe this framework will help maintaining long-term sustainability of PRGT resources, which is critical given the uncertainty over the future demand for concessional resources. To ensure that the PRGT has enough loan resources, we welcome the recent pledges and call for a wide mobilization of creditors.

39. We welcome the comprehensive reform of the Fund's lending facilities and financing framework for low-income countries that became effective last January with a new architecture that is more flexible and tailored to the increasingly diverse circumstances of LICs. This overhaul should increase the efficiency of the financial facilities for LICs and will contribute to poverty reduction and foster growth. Further consideration should be given to enhance the ability of the Fund to help LICs to cope with unexpected or adverse shocks.

40. Better targeting access to the scarce resources for concessional Fund financing to the most in need is critical. In this respect, we welcome the recent approval of a new framework for determining which member countries are eligible for using IMF concessional financial resources under the Poverty Reduction and Growth Trust. In particular, we support updating on a bi-annual basis the list of countries that will benefit from concessional resources.

41. We welcome the recent modification of the IMF/World Bank debt sustainability framework (DSF) which will help prevent the build-up of unsustainable debt while allowing adequate external development financing of LICs is a key element of. The new framework offers a more flexible approach, when necessary and possible, according to the debt vulnerabilities and macroeconomic and public financial management capacity of the countries concerned. The adaptation of the conditionality requirements will enable to meet the needs of LICs without jeopardizing long-term debt sustainability. Coordination with official and private creditors that do not apply the DSF in their lending decisions needs to be improved, as should the debt management capacity in LICs.

Non-cooperative jurisdiction

42. EU countries remain strongly committed to reinforced action towards uncooperative and non-transparent jurisdictions that lack compliance with agreed international standards in the areas of taxation, financial supervision and anti money laundering and combating the financing of

terrorism. In the prudential field, we support the work undertaken to identify the systemically most important non-cooperative jurisdictions and the use of a toolbox of positive and negative incentives, subject to proper continuous updating, and are committed to cooperate fully in the review process to ensure high compliance and transparency. We also support the public listing of incompliant and/or non-cooperative jurisdictions and, if necessary, application of counter-measures.