International Monetary and Financial Committee

Twenty-Fifth Meeting
April 21, 2012

Statement by Mr. Guido Mantega
Minister of Finance of Brazil

On behalf of the Constituency comprising Brazil, Colombia, Dominican Republic, Ecuador, Guyana, Haiti, Panama, Suriname and Trinidad and Tobago

Statement by Mr. Guido Mantega
Minister of Finance of Brazil

On behalf of the Constituency comprising Brazil, Colombia, Dominican Republic, Ecuador, Guyana, Haiti, Panama, Suriname and Trinidad and Tobago

International Monetary and Financial Committee
April 21, 2012

International Economic Outlook

1. The IMFC is meeting again in a period of exceptional economic and financial uncertainty. It is true that the outlook has improved somewhat since the end of last year, but this is no reason for complacency. We have ahead of us enormous challenges to foster inclusive growth, job creation and make further progress in poverty reduction. We also need to work to ensure fiscal sustainability, especially in advanced economies, and to better regulate and supervise the financial sector to avoid the buildup of new tensions or the resurgence of the kind of vulnerabilities experienced in recent years in the United States and advanced Europe.

2. Growth forecasts for 2012 and 2013 remain well below pre-crisis rates, with the euro area expected to drop back into recession this year. IMF projects that emerging market and developing economies will grow more than four times faster than advanced economies in 2012 and three times faster in 2013.

3. Geopolitical tensions are a new destabilizing factor to the world economy. Recent developments related to disruptions in Iranian oil exports could trigger a spike in oil prices, putting the global recovery at jeopardy. Economic sanctions, especially unilateral ones, tend to be counter-productive. We urge all the parties involved to maintain dialogue in a constructive spirit and welcome recent signs of progress in negotiations.

4. A particular concern is the looming job crisis. High levels of unemployment and underemployment are by no means a new phenomenon in developing countries. In many advanced countries, however, high unemployment, including longer-term, is a problem that a whole generation has never really experienced. In the European Union, unemployment currently affects more than 10 percent of the labor force, exceeding 20 percent in a few cases. Youth unemployment rates are even higher, reaching as much as 50 percent in Spain and Greece. Economic and social policies need to address this problem more forcefully, including by increasing the employment-intensity of GDP growth.

5. The most important short-term risks to international stability continue to lie in the periphery of the euro area. A number of economies are experiencing the painful combination

of fiscal adjustment with “internal devaluation”. This has led in some cases to a vicious cycle where falling wages and prices combined with cuts in spending and increased taxation trigger a deeper contraction in economic activity, further undermining fiscal sustainability and the stability of the financial sector.

6. The euro area authorities have been acting on several fronts to attempt to stabilize their economies and contain contagion. I welcome the recently announced increase in the euro area firewall. These recent measures will need to be reassessed as the crisis unfolds.

7. Fiscal consolidation is weighing on growth in many advanced economies. We agree with the Fund that those advanced economies with sufficient space should slow the pace of fiscal adjustment and let automatic stabilizers operate. Some of them could even introduce some fiscal stimulus. Germany and other Northern European countries, for example, may be able to adopt more flexible fiscal policies. This would not only help global demand but also facilitate the rebalancing within the euro area.

8. Some economies are paying a high price for the ultra-loose monetary policies in advanced economies. The increase in global liquidity very quickly finds its way into emerging market economies, especially the ones with stronger economic fundamentals, such as Brazil. The Brazilian government remains committed to doing whatever it judges necessary to contain excessive and volatile capital inflows through a combination of intervention in spot and future exchange markets, macroprudential measures and capital controls.

9. The IMF has given strong endorsement to the monetary policies in advanced countries, including the recent measures taken by the European Central Bank. It has been more reluctant, however, to support the defensive measures that some emerging economies are being forced to deploy in response to spill-over effects of these policies. Capital account management policies have yet to be fully accepted by the Fund as a normal part of economic policy toolkit.

Quota and Voice Reform in the Fund

10. It is often repeated that quota and voice reforms are crucial for the legitimacy and effectiveness of the Fund. The mere ritual repetition of this sort of statement is not nearly enough. Progress on this front has been limited and slow.

11. We are deeply concerned about the slow implementation of the 2010 quota and governance reforms. As agreed by the Board of Governors, these reforms should come into force no later than the Annual Meetings of 2012. We have six months left and are still very far from reaching the required super-majorities. Most of the countries of our constituency have done their part. Out of our nine countries, only one still needs to consent to the quota increase and two have yet to accept the Board reform amendment to the Articles of Agreement. The other seven countries have completed both steps.

12. We look forward to an early agreement on the main elements of a simple and transparent quota formula that better reflects members' relative economic weights. As stated in past G-20 and IMFC communiqués, "the distribution of quota shares should reflect the relative weights of the Fund's members in the world economy, which have changed substantially in view of the strong growth in dynamic emerging market and developing countries". Taking a step further, the G-20 leaders in Seoul in November 2010 committed to "continuing the dynamic process aimed at enhancing the voice and representation of emerging market and developing countries, including the poorest, through a comprehensive review of the quota formula by January 2013 to better reflect the economic weights; and through completion of the next general review of quotas by January 2014".

13. Quotas are by far the main determinant of voting power in the Fund. Thus, any quest for legitimacy at the institution should start by establishing a quota formula that is essentially based on GDP. We should not try to reinvent the wheel. Relative weights are better measured by shares in world GDP. This is the only way to align the ranking of members' quota shares and voting power with the ranking of economies by size.

14. Historically, quota formulas have served as a means to artificially boost the quota shares of advanced open economies. This has especially benefited Europe. The flaws of the current formula become apparent when some of the outcomes it entails are spelled out. For instance, Brazil's economy is larger than that of any European country but Germany and France – even with GDP measured at market exchange rates. Yet, Brazil's calculated quota share is equivalent to that of the Netherlands and smaller than those of Spain, Italy and the United Kingdom. The latter's calculated quota share, for instance, is twice that of Brazil's.

15. The current formula generates numerous other counter-intuitive results. For example, the calculated quota share of Luxemburg is larger than the one of Argentina or South Africa. The quota share of Belgium is larger than that of Indonesia and roughly three times that of Nigeria. And the quota of Spain, amazing as it may seem, is larger than the sum total of the quotas of all forty-four Sub-Saharan African countries. These and other anomalies are a product of the weight in the current formula of openness and variability, which are meaningless or artificial variables.

16. The comprehensive review of the quota formula is a crucial forward-looking element of the 2010 quota and governance reform. I recall, once again, that countries like Brazil, Russia, India and China only agreed to this reform, with its limited progress in terms of overall shift in voting power to developing countries, in exchange for the commitment to comprehensively review the formula by January 2013 and to complete the next general quota review a year later. The reluctance that some countries are demonstrating in following through with the agreements we have on the comprehensive review of the formula is deeply damaging to this institution and to these countries' own credibility.

Capital Flows

17. Management and staff of the Fund seem eager to provide policy advice on the management of cross-border capital flows. The approach followed not always complies with, and sometimes even ignores, guidance from the IMFC and the G20 regarding capital flow management measures. In our view, the analysis of capital flows should draw on countries' experiences and consider recipient as well as source countries.

18. So far, the Fund has focused mainly on recipient countries, downplaying the role of push factors, particularly those stemming from monetary policies in advanced countries. The G20's *Coherent Conclusions for Managing Capital Flows Based on Country Experiences* have been disregarded in recent staff papers, despite repeated calls from our chair and others in the Executive Board to take these conclusions into account.

19. Management and staff seem to agree that there is not enough accumulated knowledge on which to base sound advice to countries and even detailed guidance to IMF staff. Nevertheless, they persist in offering unsolicited policy advice. We have doubts about the quality, consistency and evenhandedness of the ongoing work on capital flow management and urge the Fund to rethink its approach.

20. I reiterate what I stated in my April 2011 IMFC statement: Brazil opposes any "guidelines", "frameworks" or "codes of conduct" that attempt to constrain, directly or indirectly, policy responses of countries facing surges in excessive and volatile capital inflows. Governments must continue to have flexibility and discretion to adopt policies that they consider appropriate to contain excessive inflows.

IMF Surveillance

21. In our view, the gaps in the surveillance framework stem mainly from inappropriate and weak implementation practices, rather than from shortcomings in its legal aspects. The Fund's surveillance has adapted relatively well to the crisis, often at the request of members. The improvements made in surveillance in recent years did not require any changes in the legal framework. We are not convinced of the need to adopt, at this juncture, the so-called integrated surveillance decision, as it is not clear how it would fundamentally contribute to enhance its effectiveness. Additionally, the excessive focus on reviewing the legal framework is likely to absorb scarce human resources and may, as a result, halt the ongoing improvements.

22. We should not lose sight of the fact that for the Fund's surveillance to be effective and to gain traction and legitimacy it is fundamental that it be evenhanded and unbiased. This will only be achieved after the institution implements reforms to enhance voice and representation of emerging market and developing countries.

23. Staff diversity along its various dimensions – education and professional background as well as nationality – is also fundamental to strengthen surveillance. On nationality, progress remains slow and insufficient. The top positions in Management and staff are still mostly held by nationals of a small group of advanced countries.

Small States

24. Our constituency welcomes the renewed engagement of the Fund with small, middle-income states. Our call last September for the Fund to do a better job in listening to the views of authorities and in understanding the circumstances of each country, whether big or small, seems not to have been in vain. The high vulnerability of small states to natural disasters and external shocks, as well as the constraints imposed by their size, require specific attention. We reiterate our call on the Fund to deepen its level of commitment regarding the provision of adequate resources and the development of policies tailored to these countries' peculiar circumstances.

25. In response to the concerns of our Governors, notably those from Trinidad and Tobago, Guyana and Suriname, our chair proposed the formation of an informal working group of Fund Executive Directors that represent small states. This group has been working since the beginning of this year to give greater visibility to the concerns of these countries in the IMF and to foster cooperation on issues of common interest.