



International Monetary and Financial Committee

Twenty-Fifth Meeting
April 21, 2012

**Statement by Jun Azumi
Minister of Finance, Japan**

On behalf of Japan

**Statement by the Hon. Jun Azumi,
Minister of Finance of Japan
and Governor of the IMF for Japan
at the Twenty-Fifth Meeting of the International Monetary and Financial Committee
Washington, D.C., April 21, 2012**

I. THE JAPANESE ECONOMY AND THE GLOBAL ECONOMY

The Japanese Economy

Around one year has passed since the Great East Japan Earthquake that occurred on March 11 of last year. I would like to use this occasion to express our appreciation again for the kind support we have received from countries and people around the world.

Last year, Japan recorded negative growth due to the combined effects of various factors, including the disastrous earthquake, the yen's sharp rise, a decline in external demand, and the floods in Thailand. The economy has recently been recovering moderately. For example, the Industrial Production Index, which had dropped sharply immediately after the earthquake due to the impact of supply chain disruptions, has rapidly recovered, albeit with a temporary drop caused by the floods in Thailand, and this index is now approaching pre-earthquake levels.

In addition, on the fiscal front, Japan has taken quick action to deal with the disaster, for example, by appropriating funds totaling 18 trillion yen (equivalent to approximately 4 percent of GDP) for post-earthquake reconstruction expenditures. Looking forward, we expect that the intensive implementation of reconstruction measures will steadily increase demand and create jobs. Therefore, led by expanding domestic demand, in the current fiscal year, the Japanese economy is expected to recover moderately and record real growth of 2.2 percent. At the same time, we are vigilant against risks, such as a resumption of the yen's sharp rise, a downturn in overseas economies due to the possible resurgence of the European sovereign debt crisis, and persistently high and volatile oil prices.

Japan's Fiscal Consolidation

Along with steady post-earthquake reconstruction, fiscal consolidation is a top immediate priority for Japan. In its analysis in the World Economic Outlook, the IMF points out, as a global risk factor, the possibility that an erosion of confidence in Japan's fiscal position could have negative spillover effects on the global financial markets. We recognize that steady implementation of fiscal consolidation measures that are sufficient enough to maintain market confidence is an important task that we must accomplish, without delay, for the sake of, not only our domestic economy, but also the global economy.

In order to appropriate a large budget for post-earthquake reconstruction, we secured the necessary funds by temporarily raising individual and corporate income tax rates, reducing

expenditures, and increasing non-tax revenues, without relying on the issuance of deficit-covering government bonds, based on the principle of not leaving a financial burden to future generations.

The next task is that of steadily implementing a comprehensive reform of our social security and tax systems; this reform is the centerpiece of our medium-term fiscal consolidation. In order to ensure equity between and within generations and establish a social security system that accommodates the needs of all generations, and to secure a stable source of revenue that will enhance and stabilize the social security system while pursuing fiscal consolidation, last February, the Japanese cabinet decided on the Outline of the Comprehensive Reform of the Social Security and Tax Systems and, on March 30, submitted a bill to the Diet for the fundamental reform of the tax system. This bill includes raising the consumption tax rate in two phases, from the current 5 percent to 10 percent, by October 2015, and using all additional tax revenues from the consumption tax hike for social security spending.

While steadily implementing this reform, Japan aims to create a budget structure that enables the country to achieve our goals of halving its primary budget deficit to a GDP ratio by FY 2015, compared with the FY 2010 level, and turning this deficit into a surplus by FY 2020, according to our commitment at the G-20 Summit in Toronto. I believe that such efforts will support economic growth by dispelling uncertainty over our future prospects.

The Global Economy

There are some encouraging signs for the global economy. Recently, financial markets have regained stability due to decisive European policy actions, such as southern European countries' implementation of fundamental fiscal consolidation measures, the EU's tightening of fiscal discipline, the ECB's accommodative monetary policy, and the adoption of a second rescue package for Greece. The U.S. economic recovery, as well as the strong commitment to monetary easing by central banks of advanced countries, has also contributed to the stability of the financial markets. Even though concerns remain over a slowdown in emerging economies, including Asian economies, we recognize that these economies are generally solid, supported by strong domestic demand and sound macroeconomic management.

However, we believe that there are considerable downside risks for the global economy, the main one being the European sovereign debt crisis, as indicated by a renewed upward trend in the yields of sovereign bonds issued by some euro area countries. Policymakers of individual countries should avoid slipping into complacency and exploit the temporary breathing space that was acquired by the efforts made so far for the purpose of building the resilient economic, fiscal, and financial systems that are needed to forestall future crises. When reforming the financial system, it is necessary to pay sufficient attention to the risk that a strengthening of regulations in one country could have unintended consequences on other countries. Moreover, while it is important for European financial institutions to strengthen their capital bases, it is necessary that they carefully determine the way and sequence of capital base strengthening in order to avoid causing a disorderly deleveraging and generating adverse effects on the real economy.

II. STRENGTHENING OF THE INTERNATIONAL FINANCIAL ARCHITECTURE

For the global economy to achieve stable growth, it is important to strengthen the international financial architecture, which is the global economic and financial infrastructure. The IMF plays a central role in this, and Japan has actively involved itself in the strengthening of the IMF's functions and has presented recommendations for that purpose. Regarding the IMF quota and governance reform, which was agreed upon in December 2010, Japan, last August, completed parliamentary procedures for both the quota increase and the amendment of the Articles of Agreement. As of now, only about 70 countries, holding about 45 percent of voting power, have accepted the amendment. In order to make steady progress in the discussions on the next quota review, as agreed, it is important to put into effect the 2010 IMF reform by the Annual Meetings to be held in Tokyo this October. We request countries that have not yet completed the necessary domestic procedures for the quota increase and the amendment to speed up their process.

Following, I would like to address important tasks that must be accomplished so as to strengthen the international financial architecture, such as the enhancement of the global financial safety net (GFSN), the improvement of the IMF's surveillance function, and IMF governance reform.

Enhancement of the GFSN

1. Increase in IMF Resources

To prepare for a possible future crisis amid the continuing uncertainty over the global economy and financial markets, enhancing the GFSN is an urgent task. The GFSN has a multilayer structure comprised of financial safety nets at the global, regional, bilateral, and national levels, and it is important to strengthen each safety net and, at the same time, enhance the collaboration between these safety nets.

At the global level, it is necessary to increase the Fund's resources. The euro area, with a single currency and central bank as well as strong economic power, through its own efforts, has built and strengthened its crisis response facilities, such as the European Financial Stability Facility (EFSF) and the European Stability Mechanism (ESM). On the other hand, the IMF has also provided resources to complement the firewall of the euro area and has designed and proposed necessary reforms, such as policy conditionality; thereby supporting troubled euro area countries and preventing a contagion of the crisis. Japan believes that, although not perfect, the measures to strengthen the firewall that were agreed upon by the euro area at the end of March, when evaluated together with the euro area's tightening of fiscal discipline and the ECB's long-term refinancing operations (LTROs), represent certain progress.

As the European sovereign debt crisis has not yet been fully resolved, Japan believes that, if we are to mitigate downside risks for the global economy, including Asian economies, it is important to use this opportunity to strengthen the Fund's resources so as to ensure the stability of the financial and foreign exchange markets. In light of this need, Japan believes

that it is quite important to make significant progress in strengthening IMF resources in these Spring Meetings and, based on this firm belief, on April 17, I announced Japan's pledge to contribute US\$60 billion, for a new line of credit for the IMF, in order to accelerate the process toward an agreement on this matter. At a time when the international community's unity in stabilizing the market is being tested, we strongly hope that other countries will also announce their pledges to make financial contributions to the IMF as soon as possible. At the same time, needless to say, we will continue to request that appropriate conditionalities be set for the use of Fund resources and that the division of roles between the euro area and the IMF be made appropriately if the IMF is to provide future support to any euro area country. We also ask euro area countries to make continuous efforts to strengthen their firewall, tighten fiscal discipline, and carry out structural reforms.

2. Regional Financial Cooperation in Asia

Japan is also pouring efforts into enhancing regional safety nets in Asia, efforts that complement global mechanisms such as those of the IMF. Regarding the Chiang Mai Initiative Multilateralization (CMIM), the regional safety net under the framework of the ASEAN+3, Japan, in cooperation with other ASEAN+3 countries, aims to further strengthen it through such measures as increasing its total size and introducing crisis prevention function at the ASEAN+3 Finance Ministers' and Central Bank Governors' Meeting to be held early next month. The strengthening of regional financial cooperation will provide a greater sense of regional ownership toward crisis prevention and resolution efforts, and enhance the GFSN by complementing global mechanisms such as the Fund's.

In addition, the ASEAN+3 is also striving, not only to strengthen the CMIM, but also to enhance regional surveillance functions. We hope that cooperation will be deepened further, in areas such as economic surveillance between the IMF and the ASEAN+3 Macroeconomic Research Office (AMRO), established last April as the macroeconomic surveillance unit of the CMIM.

Moreover, Japan is also strengthening its financial cooperation at a bilateral level. The currency swap arrangement with South Korea was enhanced last October, from a maximum amount of US\$13 billion to US\$70 billion, as a temporary measure, including yen-won swaps between the Bank of Japan and the Bank of Korea. Last December, Japan also agreed on increasing the maximum amount of a currency swap arrangement with India, from US\$3 billion to US\$15 billion. In addition, last December and this February, Japan and China agreed to promote financial transactions through mutual cooperation in the financial market and to work together to strengthen financial safety nets.

These regional efforts in Asia are expected to mitigate spillover effects from other regions and enhance the region's resilience by strengthening financial safety nets and promoting the use of local currencies.

Japan will continue to exercise leadership to improve financial stability worldwide and in Asia.

IMF Surveillance

Since the breakout of the global financial crisis in 2008, the Fund's surveillance function has been strengthened and this effort should be continued. In particular, it is important that the IMF conduct more in-depth analyses regarding trade and financial linkages among Fund member countries and the spillover effects of policies. From this perspective, we welcome that the Fund has started to work on an external sector report in order to conduct a comprehensive analysis regarding the external impact of other macroeconomic policies in addition to exchange rate policies and cross-border capital flows. Japan asks the IMF to fully exchange opinions with member countries about ways to improve analytical methods, as well as implement its analyses and present its results.

In addition to bilateral surveillance, multilateral surveillance covering regions and the entire world is important, so Japan supports the IMF's efforts to better integrate these two types of surveillance. We also welcome the decision to continue to prepare the Consolidated Multilateral Surveillance Report and the Managing Director's Action Plan in order to improve the consistency of the messages of IMF multilateral surveillance reports, such as the WEO, the GFSR, and the Fiscal Monitor, and to distill implications resulting from the analysis on policy measures. We believe that IMF surveillance will be made more effective if better consistency is attained between cross-country messages from multilateral surveillance and messages to individual countries from bilateral surveillance.

IMF Governance Reform

Finally, for the IMF to play the above-mentioned roles more effectively, it is essential that it make a constant effort to enhance its legitimacy, effectiveness, and credibility. First, we request that, in the ongoing reviews of quota formula and quotas, more appropriate consideration be given to member countries' capacity to make financial contributions. Since the outbreak of the global financial crisis in 2008, several financial support programs of an unprecedented scale have been adopted and, consequently, strengthening the Fund's resources has become necessary again although they have already been enhanced considerably. This indicates that in allocating quotas, which are the core element of IMF governance, the importance of a member's capacity to make financial contributions is increasing. However, the current quota formula does not satisfactorily take into consideration this capacity to make financial contributions while attaching excessive importance to financial needs, and thus it requires correction. We believe that in measuring the capacity to make financial contributions, past records of financial contributions should be taken into account on the basis of encouraging future financial contributions. Consideration should be given, not only to contributions to the New Arrangements to Borrow (NAB) and bilateral lending mechanisms that support non-concessionary lending by the IMF, but also to contributions to the IMF's important activities such as providing aid to low-income countries and technical assistance.

Increasing the IMF's staff diversity is also important so as to enhance the Fund's legitimacy, effectiveness, and credibility. Although reforms intended to match each member country's voice and quota to its relative economic weight have advanced, much room remains toward improving the staff composition. Japan is ready to make as much of a contribution to the

Fund in terms of human resources as in terms of financial resources.

III. TOWARD SUCCESSFUL ANNUAL MEETINGS IN TOKYO

Japan will host this year's IMF and World Bank Annual Meetings in Tokyo. We look forward to welcoming guests and representatives from all over the world, presenting a country restored from the earthquake and making a fresh start, just like in the last Annual Meetings that were held in Tokyo, 48 years ago.

In the forthcoming Annual Meetings, as the host country, we would like to actively make intellectual contributions by jointly holding seminars with the IMF and the World Bank on various challenges faced by the global economy. Indeed, Japan is not only carrying out post-earthquake reconstruction but also tackling many challenges, such as responding to an aging society, coupled with a decline in population, overcoming deflation, promoting growth, and implementing fiscal consolidation. We hope that the coming Annual Meetings in Tokyo will act as a catalyst for strengthening solidarity among countries around the world in order to overcome various challenges by providing an opportunity for active discussions on a broad range of issues, from fiscal and financial policies to development and disaster risk management.

At the same time, we hope that both guests and representatives will be able to gain first-hand experience of the cultural and technological power of Japan. In our preparations, we will do our utmost to extend our best hospitality and make the Annual Meetings successful.