



International Monetary and Financial Committee

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**IMFC Statement by Wolfgang Schäuble
Minister of Finance
Germany**

On behalf of Germany

Statement by Mr. Wolfgang Schäuble
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to the International Monetary and Financial Committee
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I. Global Economy and Financial Markets

The global economy is expanding at a more satisfactory pace. We can be more optimistic about the outlook than during our past meetings, with an acceleration of growth in advanced economies and good growth prospects in emerging economies. Output gaps are generally closing, and in fact are already closed in many advanced economies. The unemployment level is decreasing and some economies are already at full-employment.

However, there are still risks and reason for caution. Uncertainty, notably policy uncertainty, remains. And growth itself remains uneven across countries and regions. Global trade growth has slowed in recent years – it has slowed during the recovery, which is just when it would be expected to rise. In addition to that fact, there is also evidence of the rise of protectionism and protectionist sentiments. Trade has benefited the world economy enormously – pulling millions out of poverty, bringing prosperity and stability. Turning back the clock on globalization could harm growth substantially. It would also destabilize emerging economies – some of which have already suffered from low commodity prices, volatile currencies and fluctuating capital flows in recent years.

In response to this, Germany commits to keep the global economy open, resist protectionism and keep global economic and financial cooperation on track, including by further strengthening a rules-based international order, of which multilateral institutions and fora, and their processes, form an important part.

There is evidently a need to better communicate the benefits of trade and globalization. We need to ensure that there is equality of opportunity to benefit from economic growth and trade, and also that there are efficient measures in place in our countries to assist those who inevitably lose out due to structural changes and increased competition as a result of trade.

We also need to do more to ensure that our economies are resilient. Financial crises can have severe and long-lasting consequences: almost ten years after the beginning of the global financial crisis, we are still dealing with its aftermath. Should a future crisis occur, we have very little room for maneuver: much too high private and public debt levels are leaving no fiscal space and ultra-loose monetary policy has clearly reached its limits. Our main policy levers going forward are devising sound fiscal policies and continuing with our structural reforms, e.g. to ensure flexible and efficient product and labor markets. I am proud that the G20 has, under the German Presidency, agreed a set of resilience principles to guide us in selecting policies to make our economies more resilient. That is a first step – now we need to implement these principles in our economic policy making.

As part of building our resilience, we must address debt. Although some progress concerning the reduction of deficits in recent years and a decline in the aggregate level of government debt has been achieved in Europe, private and public debt globally is still far too high and expected progress in debt reduction is too slow. The IMF Fiscal Monitor predicts that debt in advanced economies will not be declining in 2017, averaging over 100 percent of GDP, and will stabilize at this level in the medium term. Debt overhang in many economies could become a severe obstacle for future growth or even a breeding ground for a new crisis. We must start to bring debt onto a downward path now. Only this will allow us to build buffers to respond to a future crisis.

Shifting to growth friendlier public spending and tax mix is crucial. This is why Germany has increased spending on targeted public investment in infrastructure. In fact, public investment will be the most dynamic public expenditure component according to our medium-term budgetary planning. Sustainable public finances are crucial to improve equal opportunities across generations and secure stability. The most vulnerable groups in the population benefit the most from stability, since they cannot hedge against uncertainty.

Euro area developments

The euro area continues to grow at a moderate rate, despite a high level of uncertainties within Europe (e.g. Brexit negotiations, upcoming elections in several member states) and globally (e.g. geopolitical developments). We see positive growth rates in all EU member states. Structural reforms strengthening the growth potential and the consolidation of public finances have played their part in the recovery, which has also been supported by low oil prices and the accommodative monetary policy of the ECB. Headline inflation is gradually normalizing,

mostly reflecting the recovery in oil prices, while underlying inflation is forecast to rise more slowly. Consolidation efforts undertaken over the last couple of years have led to visible results, including increased confidence, a reduction of headline deficits and debt levels for the euro area aggregate. The economic recovery continues to have positive effects on labor markets. Unemployment is on a downward trend and participation rates are increasing. Reform efforts begin to pay off.

However, several Member States still face substantial public deficits and high debt ratios, while efforts to consolidate public finances have lost momentum more recently. It remains important to raise potential growth through effective structural reforms and to reduce public debt through growth friendly fiscal consolidation and adherence to EU fiscal rules. The debt crisis clearly indicated the importance of sustainable public finances in a Monetary Union. The current environment of moderate growth and low financing costs should be used accordingly. An effective combination of structural reforms and growth-friendly consolidation will ensure the sustainability of public finances, strengthen confidence, foster employment and increase the euro area's long-term growth perspectives.

Germany

Germany continues on its growth path with positive growth forecasts for 2017 and 2018 (calendar adjusted 1.7 % for 2017, 1.6 % for 2018). In particular domestic demand, both private and public, is the main driver of this dynamic. Record levels of employment and increasing wages support private consumption. However, uncertainties in the global economy require prudent fiscal policies to contribute to stability.

The German fiscal position remains sound. Germany last year for the third time in a row generated a general government surplus (+0.8% of GDP). On the one hand, pressure on government budgets was eased by favorable economic developments and by interest expenditure falling again. On the other hand, the underlying fiscal stance was still expansionary. All in all, public finances benefited from significant revenue increases; revenue as share of GDP now exceeds 45% of GDP and is at a multiyear high. However, expenditure also increased steeply in many cases, mainly due to the provision of support for refugees, but also with regard to pensions and healthcare, for instance. Government budget plans also foresee higher spending on public investment – with increases of around 5 percent each year until 2021. As a consequence, fiscal policy will continue to remain moderately expansionary.

The debt ratio is likely to decrease further in the coming years: The general government budget is projected to be balanced until 2021; the debt-to-GDP ratio will continue to fall below 60%. Rising social spending, driven by demographics in Germany, presents a continued argument for rapidly scaling back the government debt ratio, to make our budget generationally fair and more resilient towards adverse events.

Enhancing resilience also hinges on whether the state guarantees equal opportunities for its citizens and incentivizes him or her to be active. Because of effective public redistribution schemes and generally no-cost education systems, Germany has one of the lowest degree of income inequality among G20 countries. Efficient budget allocation for productivity enhancement and sustainable public finances to secure social security in the long run – notably for people with lower incomes – and adaptable labor market institutions to help achieve high employment turn out to play key roles for inclusive growth in Germany.

Financial Sector

In spite of the improved economic outlook, low interest rates and modest growth in some regions of the world pose a significant risk to financial stability. The market environment for financial institutions remains challenging. In particular, profitability of financial institutions has severely been squeezed over the last years and many banks and insurance companies will have to adapt their business models in the medium term.

At the same time, new sources of risks, such as the potential of increasingly inward-facing policies, have begun to emerge. Underperformance of reforms or unexpected political events might lead to an abrupt repricing of assets.

The achievements of the last years in stabilizing financial markets have to be safeguarded. Only a well-monitored and responsibly regulated financial sector will be resilient enough to provide a sound basis for sustainable growth. Therefore, we should remain committed to support the timely, full and consistent implementation of the agreed financial sector reforms. Any hasty and uncoordinated rollback of regulation, which could jeopardize financial stability and result in increased financial fragmentation, should be averted.

Accelerating technological change is affecting consumer preferences and consumer behavior and increases pressure on incumbent financial firms, including with respect to core functions such as credit supply, the provision of payment services and asset management services. At

the same time, the use of financial technology may help financial institutions lower operational costs and thereby raise profitability. The rising digitalization of distribution channels and customer's appetite for "always-on" services also presses for adaptation, whereas many institutions still rely on ageing core IT-systems, which raises concerns about operational risks. Within this new digital environment, cyber risk appears as a major risk, which has to be addressed internationally.

In Europe the issue of non-performing loans in some countries needs to be addressed in a comprehensive manner in full respect of the existing rulebook. Within a period of subdued growth, low interest rates and relatively high debt levels in some countries, stability concerns may rise in the medium term, especially if interest rates would rise. Rising costs of credit could bring back the topic of unsustainable debt levels to the international agenda, both to advanced and emerging economies.

At the global level, it is important to maintain a spirit of cooperation in international finance, both to foster efficiency and growth, and to protect our financial systems from new stability risks.

International Taxation

It is crucial to further develop a fair and growth friendly international tax system. Isolated tax policies are no longer sufficient. Scandals about undeclared assets held abroad or aggressive tax planning strategies by certain multinationals have shown how inconsistencies between different countries' tax rules and a lack of cooperation among tax administrations can leave room for unwarranted tax planning and tax evasion.

With the valuable assistance of the OECD, the G20 has established new global standards for tax transparency, putting an end to bank secrecy. Moreover, the G20 has agreed on concrete measures to eliminate harmful tax competition and aggressive tax planning. Under the Inclusive Framework on BEPS, more than 90 countries have joined forces to address base erosion and profit shifting. The G20 has also been careful to take the specific needs of developing countries into account. Good progress has been made and international cooperation will be further intensified. In this context, the G20 has asked the OECD to deliver a progress report on enhanced accessibility of beneficial ownership information and to prepare a list of those jurisdictions that have not yet sufficiently progressed towards a satisfactory level of implementation of the agreed international standards on tax transparency by the Hamburg Leaders Summit in July 2017.

In addition, the G20 decided under Germany's G20 presidency to add new tax topics to its agenda. During the meeting of the G20 finance ministers and central bank governors in Baden-Baden in March, possible ways to enhance tax certainty were discussed. There was general agreement that tax uncertainty has detrimental effects on both governments and taxpayers. Furthermore, intensive discussions were held on the implications of the spread of digital technologies for taxation. Rapid evolution of information and communication technology fundamentally alters business models and the way in which value is created.

II. International Financial Architecture and IMF Policies

Capital Flows

How to best combine the merits of free capital flows with the need for stability of the financial system remains on the forefront of the international agenda. Germany welcomes that the IMF has continued to explore the diverse issues surrounding capital flows. The present focus on the interaction between capital flow measures and macroprudential measures is apt and should be continued. Germany believes that the IMF and the OECD should strive to continue to have consistent assessments of both kinds of measures, in order to increase transparency for the international community. We also commend the efforts of the IMF to improve the empirical basis for these issues, through the establishment of a macroprudential database that will be open to researchers around the globe, as well as through the Fund's engagement in the Data Gaps Initiative II. All these efforts should result in a deeper knowledge about the functioning as well as the respective benefits and costs of both capital flow and macroprudential measures and will help make the International Monetary System more resilient.

GFSN

An adequate Global Financial Safety Net (GFSN) that contributes effectively to crisis prevention and resolution is a key component underpinning the stability of the international monetary system. Nevertheless, the GFSN – however strong – cannot substitute for necessary efforts at the national level. Resilience against crises is first and foremost a national responsibility, grounded in sound domestic policies. It would therefore be unwise – and even counterproductive – to create expectations of ever-expanding coverage and insurance under the GFSN. The safety net architecture has evolved and expanded considerably in recent years; today it is financially as strong as never before. At the same time, its diversity allows for flexible and tailored responses to crisis developments. The IMF is the only truly global element of the

GFSN, offering a uniform and non-discriminatory safety net for all member countries in case of a balance of payments need. Regional Financing Arrangements and foreign reserves apply at the regional or national level. As Germany is committed to a well-functioning GFSN, we support the work streams currently underway to further strengthen its architecture, with a strong, quota-based and adequately resourced IMF at its center. To that end, we welcome the efforts to intensify cooperation between the IMF and regional financing arrangements and look forward to reviewing the IMF's lending toolkit to further enhance its effectiveness and address concerns about the prolonged use of precautionary facilities. The conclusion of the toolkit review will help assessing the resource needs and appropriate size of the IWF, which should be the basis for the further discussion on the 15th General Review of Quotas. A plausible and credible perspective for a possible quota increase would need to be the material precondition for the ensuing discussion about the quota formula and quota distribution.

IMF-RFA Cooperation

We support work to assess the cooperation between the IMF and RFAs and welcome the efforts made in this direction, as was exemplified by the test run conducted between the IMF and the CMIM. Allowing for adequate consultation with all stakeholders will be important in this process. Given that aims and mandates vary considerably between RFAs, there is no one-size-fits-all approach to IMF and RFA cooperation.

Lending Toolkit

As regards the current review of the IMF's toolkit, Germany looks forward to the presentation of well thought-through reform proposals and their discussion in the Executive Board in the near future, including on a possible new liquidity support instrument and reforms of existing instruments to address concerns about prolonged use. Ensuring well-designed instruments is of key importance. This includes having a clear purpose in line with the IMF's mandate and its resource envelope, maintaining appropriate incentives for sound domestic policies as well as safeguarding the integrity of Fund resources. The principles governing IMF lending, which are embedded in its Articles of Agreement and have served the Fund well over many years, should guide this work. These include the revolving nature of Fund resources, which implies that resources are being made available only on a temporary basis to become available again for other members if needed. Another important IMF principle is to ensure adequate safeguards for Fund resources. While prequalification can substitute to some degree for program conditionality and may contribute to reducing a perceived 'stigma' of the IMF, criteria need to

be sufficiently strong. Critically, the review of the lending toolkit should take into account recent experiences with precautionary instruments, including addressing challenges, such as the prolonged use of the FCL instrument and the unresolved challenge of establishing stronger incentives for a timely and credible exit strategy. Finally, while the temporary use of precautionary Fund lending facilities can be a component of an effective GFSN, they should not jeopardize the Fund's financial capacity for its regular adjustment programs to address acute balance of payments needs of member countries – a core function of the IMF and an area where the Fund has unique global expertise to offer.

Improving Debt Sustainability

With a view to ensuring debt sustainability in the world economy with many countries facing high or rising public debt levels, the Fund can play an important role in advising countries on their debt policies.

G20 Finance Ministers and Central Bank Governors welcomed the Operational Guidelines for Sustainable Financing reflecting responsibilities of both borrowers and lenders. The Operational Guidelines recognize the importance of the IMF's Debt Limit Policy, the Fund's provision of technical assistance to debtor countries, its role as a venue for dialogue between sovereign creditors, debtors and financial institutions, and welcome the ongoing work aimed at strengthening the Debt Sustainability Framework. In this context, Germany strongly supports discussions about sovereign debt issues in the Paris Club and in the Paris Forum.

Debt sustainability can also be supported by an appropriate choice of debt instruments. In this context, GDP-linked bonds and other state-contingent debt instruments might play a useful role to enhance the resilience of economies. We thank the Fund for its comprehensive analysis of this category of debt instruments for sovereigns, taking into account experiences with previous issuances of state-contingent instruments as well as feedback received in consultations with issuers and investors. To help guide interested authorities in this area, a Compass for GDP-linked Bonds was developed under the German G20-Presidency and recognized in Baden-Baden, which provides an overview of important aspects of the instrument, listing benefits, challenges and their potential mitigating factors, as well as considerations on instrument design. This work could be taken up by the Fund in its advisory role to support countries in their efforts to ensure debt sustainability.

Some General Remarks on IMF Resources

It is noteworthy that the IMF's overall lending capacity and liquidity are maintained at a very high level, and thereby, the Fund is fully-equipped to meet members' needs in times of persistent elevated uncertainties. Besides its large quota resources, the Fund continues to be in the position to take recourse also to borrowed resources, the NAB and bilateral borrowing agreements as a third line of defense, if needed and under specified circumstances. We very much welcome the 31 new bilateral borrowing agreements worth SDR 279 billion that have been approved by the Executive Board since the Annual Meetings last year. Additionally, SDR 20 billion of the 2016 round will be agreed with the Fund pending on domestic approval processes in individual countries.

Sovereign Debt Restructuring

Germany welcomes the Fund's work concerning sovereign debt restructuring and its efforts to strengthen the existing contractual market-based approach in order to facilitate efficient and effective sovereign debt restructuring measures. As we strongly support the IMF's important contribution to encourage the broad use of modified pari passu and enhanced collective action clauses (CAC) in new public debt issuances, further progress is being discussed in the International Financial Architecture (IFA) Working Group during the German G20 presidency.

Compact with Africa

To promote global growth and employment generation, the German G20 Presidency launched a G20 Africa Partnership. One key element of the partnership is the Compact with Africa Initiative, which aims to support private investment, including in infrastructure, in Africa. It strengthens collaboration between interested African states, International Financial Institutions, and other partners to improve the framework conditions for private investors. Five African countries have been the first to join the initiative, Cote d'Ivoire, Morocco, Rwanda, Senegal, and Tunisia. They have started discussing concrete measures and instruments to improve the conditions for private investment to be included in individual investment compacts, which will be finalized and presented at the G20 Africa Partnership conference in June in Berlin.

Sustainable Development and Financing for Development

Besides supporting private investment, domestic resource mobilization is of utmost importance for sustainable financing and development. Remittances are another factor of own resources,

not only for private consumption, but also for private investment, in particular in small and medium-sized enterprises. To guarantee a safe, well-regulated, but also adequately priced flow of remittances, further issues relating to remittance providers, including their access to banking services, must be dealt with. An enhanced dialogue between the public and the private sector as intensified during the German G20 presidency can help to identify any remaining issues in order to improve the environment of remittances.

We would also like to highlight the importance of the Fund's Capacity Development in this regard. IMF Capacity Development priorities are well aligned with the above-mentioned goals, including fostering resource mobilization, financial inclusion, and institution building in fragile states. Germany continues to be an important donor to IMF Capacity development, contributing to Regional Technical Assistance Centers, especially in Africa and the Middle East, and to different topical Trust Funds including the Tax Policy and Administration Topical Trust Fund, which Germany chairs.

The IMF has an important role to play in supporting Low Income Countries. In assisting these countries on their path to structural reforms and better economic policies the Fund regularly helps to catalyze financial support from other multilateral and bilateral donors.