

IMF EXECUTIVE BOARD DISCUSSION OF THE OUTLOOK, MARCH 2011

The following remarks by the Acting Chair were made at the conclusion of the Executive Board's discussion of the World Economic Outlook on March 28, 2011.

Executive Directors noted that the global recovery is gaining strength, though at varying speeds across countries. Many advanced economies that had been at the center of the global crisis and/or had large precrisis imbalances continue to experience relatively sluggish growth and elevated unemployment rates. Growth in many emerging market and developing economies has been robust, with signs of overheating in a number of countries. While remaining vulnerabilities have yet to be fully addressed, new challenges are emerging, pointing to the urgency of pursuing more vigorously the policies needed to build a more balanced and robust global economy.

Directors observed that, while the prospects for global recovery have solidified, downside risks continue to prevail. These emanate from high unemployment, still-weak sovereign and financial balance sheets, and vulnerable real estate markets in many advanced economies. Meanwhile, rising oil, food, and commodity prices, developments in the Middle East and North Africa, and the recent earthquake in Japan have further amplified the challenges. On the upside, a stronger pickup in corporate sector activity in some advanced economies and, over the near term, buoyant demand in emerging market and developing economies could propel global growth further.

Directors underscored the importance of faster progress in strengthening government and financial sector balance sheets in many advanced and some developing economies. Improving economic conditions provide a good opportunity to implement fiscal consolidation plans and entitlement reforms—supported by strong fiscal frameworks and institutions—and place public debt on a sustainable path. With the pace of fiscal consolidation slower than

anticipated for 2011 in key advanced economies, clearer, more detailed medium-term adjustment strategies are all the more important to reestablish fiscal credibility. Financial sector repair and reform also need to be accelerated on all fronts to restore confidence. The focus should be on rigorous stress testing, further bank restructuring and recapitalization, and rebuilding stronger mortgage credit and securitization markets. A further priority is to fill persistent gaps in financial sector supervisory and regulatory frameworks, addressing risks posed by shadow banking systems and “too-important-to-fail” institutions and inadequate cross-border resolution frameworks.

Directors generally agreed that, in advanced economies with strong central bank credibility and well-anchored inflation expectations, monetary policy could remain accommodative while the much needed fiscal consolidation and financial sector reforms proceed. In some countries, however, risks to price stability deserve closer attention. While unconventional measures designed to deal with specific financial market tensions could continue to be maintained in the near term, their implications for bank restructuring should be carefully assessed.

Directors emphasized that many emerging market and developing economies need to be vigilant for overheating pressures and inflation risks stemming from food and energy prices, which weigh heavily in consumption baskets, as well as from the rapid recovery in domestic credit. For countries with external surpluses and no fiscal concerns, the priority would be to unwind monetary accommodation and allow stronger currencies to anchor inflation expectations, which will also assist external rebalancing. Those with external deficits should tighten both fiscal and monetary policies. In addi-

tion to macroeconomic adjustment, economies experiencing booms in credit and asset markets could adopt macroprudential policies to maintain financial sector strength and stability, complemented by other measures to manage capital inflows where deemed necessary.

Directors recognized that, because countries are at different stages of recovery and cyclical positions, their monetary policy responses necessarily differ, widening interest rate differentials among countries. Beyond domestic factors, global financial conditions help explain the variability of cross-border capital flows. Directors noted the IMF staff's conclusion that, as long as accommodative monetary policies help stabilize output in advanced economies, spillovers to emerging and developing economies would be, on the net, beneficial. At the same time, many Directors drew attention to the effects of prolonged loose monetary policy in major advanced economies, and risks of a sudden reversal, on global capital flows. They viewed these developments as further complicating macroeconomic policymaking in many capital-recipient countries, underscoring, in the view of some Directors, the case for international monetary coordination.

Directors noted that the persistent rise in oil prices reflects both increased scarcity of supply

and rapid growth in oil consumption. Although gradual and moderate increases in oil scarcity are not expected to pose a major constraint on global growth in the medium to long term, uncertainty remains high and the potential for abrupt shifts cannot be ruled out. Directors saw merit in further analysis and discussion on the range of policy options to facilitate adjustment. They stressed the need for policymakers to pay attention to social challenges arising from elevated prices of food and commodities, with the first priority being the development of well-targeted social safety nets to protect the poor.

Directors underscored that the continuing improvement in global economic and financial health should not diminish the urgency for completing the policy reform agenda. Decisive further progress in fiscal and financial sector adjustment, the removal of distortions that hold back global demand rebalancing, and tighter macroeconomic policies where inflation pressures are building are all key to sustaining healthier, more balanced global growth. While these policies are in the interest of each individual country and action should not be delayed, continued coordination and joint initiatives will facilitate more ambitious policy adjustments and stronger outcomes.