IMF EXECUTIVE BOARD DISCUSSION OF THE OUTLOOK, APRIL 2015

The following remarks were made by the Chair at the conclusion of the Executive Board's discussion of the World Economic Outlook, Global Financial Stability Report, *and* Fiscal Monitor *on April 3, 2015.*

Executive Directors noted that a moderate recovery continues in the global economy, with uneven prospects across countries and regions. Growth in emerging market economies is softening, reflecting an adjustment to weaker medium-term growth expectations, lower commodity prices and exports, and country-specific factors. The outlook for advanced economies shows some signs of improvement on the back of lower oil prices, continued support from accommodative monetary policy stances, and some moderation in the pace of fiscal adjustment. A number of Directors considered that global economic developments might turn out to be more positive than currently expected. A few other Directors emphasized the importance of decisive policy actions to counter the "new mediocre."

Directors noted that global growth should continue to increase gradually as crisis legacies fade and advanced economies benefit from accommodative macroeconomic policies. Emerging market economies are likely to slow further in 2015, but growth should pick up again in 2016 and beyond, as the current setbacks to activity begin to dissipate. Directors agreed that the near-term distribution of risks to global growth has become more balanced, although most noted that it remains tilted to the downside. The decline in oil prices could boost activity more than expected, but geopolitical tensions continue to pose threats, and risks of abrupt shifts in asset prices—including exchange rates—have increased. In some advanced economies, protracted below-target inflation or deflation could affect activity and public and private debt dynamics. A few Directors considered that this risk has diminished. A few others urged greater focus on global imbalances.

Despite the expected improvement in the outlook, Directors broadly agreed that short-term financial stability risks have increased. Oil- and commodity-exporting countries and firms generally face revenue losses and higher risks. Emerging market corporations that have borrowed heavily in U.S. dollars and are not sufficiently hedged are now faced with potential balance sheet pressures from the appreciating U.S. dollar. A retrenchment of overinvested industries and property price declines—especially in China—could spill over to emerging markets more broadly. In advanced economies, the low-interest-rate environment poses challenges for long-term investors, including weaker life insurance companies in Europe. High debt levels and nonperforming loans in the private sector continue to pose headwinds to growth and financial stability in some advanced economies. Recent declines in liquidity in some markets may amplify financial stability risks.

At the same time, Directors also noted important medium-term risks to the global recovery. In emerging market economies, tighter financial conditions or unaddressed supply-side constraints represent significant risks. Growth prospects in advanced economies are held down by aging populations, weak investment, and lackluster productivity growth while sustained weakness in demand could weigh on potential output.

To address these risks and challenges, Directors underscored that boosting actual and potential growth remains a policy priority. In emerging market economies, macroeconomic policy space to support growth remains limited, but lower oil prices will alleviate inflation pressures and could increase fiscal space in oil importers. In oil exporters, adjusting public spending in view of lower fiscal revenues is a priority, although countries with strong financial buffers may adjust more gradually. Better fiscal frameworks with clear medium-term objectives are needed in many countries to anchor fiscal policy and avoid a procyclical policy stance. Directors also emphasized that lower oil prices provide an opportunity to reform inefficient energy subsidies and provide breathing room for more productive and equitable spending and growth-enhancing tax reforms.

Directors broadly concurred that continued accommodative monetary policy is essential in many advanced economies. To support credit markets, additional measures are needed to restore balance sheet health in the private sector, including in the euro area. At the same time, many Directors noted the limitations and risks of prolonged accommodative monetary policies and divergent monetary stances, and some underscored the need to better understand their implications for emerging market and developing countries. Fiscal policy could be used to support demand and contribute to global rebalancing, for example through infrastructure investment in some advanced economies, while countries constrained by high levels of public debt should pursue growth-friendly reforms affecting the composition of revenues and expenditures. Credible medium-term fiscal consolidation plans are still needed in a number of countries, especially in Japan and the United States.

Directors highlighted the importance of a sound international banking system, and noted that more progress on the implementation of regulatory standards and cross-border resolution is needed. Strengthening microprudential policies and building a macroprudential toolkit remains a priority in many emerging market and developing economies. In advanced economies, the oversight of certain parts of the nonbank financial sector needs to be strengthened, particularly the asset management industry, as well as the life insurance industry in Europe, with better microprudential supervision and stronger emphasis on systemic risk. A number of Directors noted progress in the international regulatory reform agenda and increased efforts to monitor financial risks and build resilience. They cautioned that additional regulation and oversight should be commensurate to the systemic risk posed and take into account both costs and benefits.

Directors emphasized the importance of exchange rate flexibility for emerging markets without currency pegs, while recognizing that measures may be necessary to limit excessive exchange rate volatility. Bolstering resilience to external shocks will also require stronger macroeconomic and macroprudential policy frameworks, and robust prudential regulation and supervision. In China, further progress to gradually shift the composition of demand toward domestic consumption and reduce reliance on credit and investment would help forestall medium-term risks of financial disruption or a sharp slowdown.

Directors called for further structural reforms to raise potential growth. In emerging market and developing economies, the main priorities are removing infrastructure bottlenecks, reforming labor and product markets, strengthening education, easing limits on trade and investment, improving business conditions, and enhancing government services delivery. In advanced economies, strengthening public infrastructure, increasing labor force participation, and enabling innovation and productivity-enhancing investment are key priorities. In the euro area, reforms need to tackle legacy debt overhang, barriers to product market entry, labor market regulations that hamper adjustment, and obstacles to investment activity. In Japan, there is scope to improve service sector productivity and support investment through corporate governance reform.

Directors also stressed that continued strong growth in low income developing countries calls for greater progress in diversification and structural transformation. Key requirements include boosting fiscal positions with stronger revenues and rationalized public spending, strengthening public financial management, achieving greater monetary policy independence, promoting financial deepening, and attracting capital flows. Infrastructure investment, anchored in well-designed debt management strategies, is essential to increase growth potential. Advanced and systemically important emerging economies should play a supportive role in maintaining an enabling external environment for low-income developing countries. Priorities include further trade liberalization, providing development aid and technical assistance, completing the global regulatory reform agenda, and cooperating on international taxation and climate change issues.