STATEMENT BY THE MANAGING DIRECTOR
OF THE INTERNATIONAL MONETARY FUND

Attached for information for the Members of the Development Committee is a Statement from the Managing Director of the International Monetary Fund, Christine Lagarde, for the Committee’s eighty-sixth meeting to be held in Tokyo, Japan, on Saturday, October 13, 2012.

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Recent setbacks to the recovery underscore the vulnerability of the global economy. The advanced countries need to respond to difficult policy challenges with comprehensive plans for fiscal sustainability and, in the euro area, by pushing ahead toward banking and fiscal union. The emerging economies face slowing growth and mounting external risks, and many have already responded by pausing or reversing last year’s monetary tightening. Growth in the low-income countries (LICs) has held up well, but—with fiscal, current account, and reserves positions weaker than in 2009—most are less well prepared to deal with external shocks. The Fund is taking actions to further enhance surveillance and to secure its capacity to provide concessional assistance to its poorest members.

I. PROSPECTS AND RISKS

The recovery has suffered setbacks and uncertainty weighs on prospects. Activity in the advanced countries has decelerated sharply amid stresses in the euro area and continued fiscal consolidation and balance sheet repair. Growth has also slowed in many emerging and developing countries—including Brazil, China, and India—owing to weaker demand from advanced countries, some policy tightening in response to capacity constraints, and a turn in the credit cycle. At the same time, falling non-food commodity prices and spikes in prices of certain food items add an extra burden to many emerging and developing countries.

While global imbalances and associated vulnerabilities have diminished, they remain a cause for concern. More adjustment in (current account) deficit countries and higher domestic demand in surplus countries would not only lower risks, but would also support more sustainable global growth.

II. MACROECONOMIC POLICY ISSUES

Country-centered policy priorities

Advanced country policy makers face deep-seated policy challenges, including overburdened private and public balance sheets. Resolving the crisis in the euro area—where immediate risks are concentrated—requires progress toward banking and fiscal union, as well as fiscal consolidation and structural reforms to boost growth and employment. In other advanced countries, a looser monetary policy is having a positive impact on financial markets, output, and employment, but the impact may be diminishing. Comprehensive plans for fiscal sustainability are needed to restore confidence.

Improved policies have raised the resilience to shocks for many emerging and developing economies. However, many emerging market countries are facing slower growth and mounting external risks, with reduced policy space. In many countries, last year’s monetary tightening is being paused or reversed—an appropriate response to a weakening outlook. Policymakers will need to respond flexibly to shocks while maintaining sound fiscal and monetary positions.
Most low-income countries (LICs) recovered quickly from the global crisis and have experienced strong growth since 2010, but vulnerabilities are re-emerging. With weaker fiscal positions, higher current account deficits, and depleted reserves, LICs are now less well prepared to deal with external shocks. Short-term risks to the global outlook are tilted to the downside and the challenge for many LICs is to use their currently buoyant growth to rebuild policy buffers without unduly compromising public investment and social protection.

The Fund and international policy coordination

Along with other partners, the Fund assists the G-20 in advancing the Framework agenda to promote strong, sustainable, and balanced growth. As part of the G-20 Mutual Assessment Process (MAP), the Fund again provided inputs to assess the global consistency of members’ policy commitments with stated growth objectives. In addition, we have been asked to help support the G-20 as they develop an accountability assessment framework as part of the MAP to assess progress toward fiscal, monetary, and structural policy commitments, identifying areas where further measures or implementation may be needed. Under the Mexican G-20 Presidency, the Fund continues to provide support for the G-20 Data Gaps Initiative and contributes to discussions to strengthen the international financial architecture and identify optimal policy responses to excessive commodity price volatility.

The global economic crisis has highlighted the role of trade liberalization as a policy tool for strong, durable growth and to reduce global imbalances. Concluding the Doha Round remains a priority, and more work is needed to overcome remaining differences. Pending tangible progress at the multilateral level, advanced and major emerging market countries could pursue unilateral trade liberalization (especially on a nondiscriminatory basis), expand and simplify trade preferences for the poorest countries, and reduce trade-distorting farm subsidies. Policymakers should reverse trade-restricting measures adopted in response to the crisis and, in dealing with the recent upswing of food prices, refrain from trade restrictions that would disrupt supply and exacerbate price increases.

While difficult times in many donor countries have put pressure on aid budgets, it is important that donors meet their aid commitments. Further increasing aid effectiveness is also important, including through enhanced capacity building.

III. Fund Support for a Durable Economic Expansion

The Fund continues to respond flexibly to the high demand for crisis financing. Reflecting in part ample and front-loaded Fund financing, streamlined conditionality, and the use of available policy space to support activity, most countries in the initial wave of crisis-related programs avoided the deep recessions and exchange rate overshooting that had characterized earlier crises; most of these countries have graduated from Fund-supported programs. With a second wave of programs, including in the euro area and the Caribbean, the experience has been more mixed. Weaker initial conditions and pervasive problems have complicated program design, delayed program implementation, and—in the case of Greece—required sovereign debt restructuring.
The Fund continues to adapt its financing instruments to members’ needs. Since the Spring Meetings, the Precautionary Credit Line (PCL) was replaced by the Precautionary and Liquidity Line (PLL). The PLL allows for greater duration flexibility and can be used by members with strong policies and limited vulnerabilities to address actual as well as potential balance of payments needs. A PLL arrangement has recently been approved for Morocco.

Addressing and containing the euro area crisis is critical not only for Europe, but also for the global outlook, and the Fund is providing financing, policy advice, and technical assistance (TA). We work independently and, particularly in the crisis countries, together with other international institutions. Beyond our role through Fund-supported programs, under which we support countries’ efforts to secure affordable financing while they undertake sustained adjustment, we are also stepping up policy advice regarding European plans for a more robust monetary union. Addressing sovereign-bank links is a priority, and financial sector assessments are a key input to our macroeconomic policy advice; we are preparing to conduct such an assessment for the European Union as a whole.

We are actively supporting the Arab Countries in Transition (ACT) as part of the international response in the region. Sustained engagement by the international community and determined efforts by the ACTs are needed to maintain macroeconomic stability and achieve each country’s medium-term vision for durable and inclusive economic growth. Accordingly, we are engaging closely with the ACTs on financial assistance, capacity building, and policy advice. In April, we supported Yemen with a $94 million concessional loan under the Rapid Credit Facility. In August, the IMF approved a $2.1 billion Stand-by Arrangement for Jordan and (as noted above) a $6.2 billion Precautionary and Liquidity Line for Morocco, in support of these countries’ economic programs. Egypt has requested an IMF arrangement and discussions are underway. In Libya and Tunisia, we are providing policy advice and assistance to build institutional capacity. We are also engaging with international partners to support the ACTs in securing the official financing, trade access, and international expertise necessary to ensure successful economic transitions.

Demand from our LIC members for concessional financing peaked at $3.8 billion in 2009 and remains high, with an average annual commitment of about $2 billion during 2010-12. Fund financial and policy support is promoting poverty reduction and growth by relieving liquidity constraints and catalyzing donor support, and enabled LICs to protect or even boost priority spending during the crisis. The Fund has also provided financial support to drought-affected countries in Africa: since 2011, programs for Burkina Faso, Djibouti, and Kenya were augmented and new programs were approved, in part due to drought-related vulnerabilities, for The Gambia, Mali, and Niger. In Asia, a $1 billion Extended Credit Facility arrangement for Bangladesh has aided macroeconomic stabilization and is laying the foundation for stronger growth. The Fund stands ready to provide additional assistance to affected countries.

Further progress has been made under the Heavily Indebted Poor Countries (HIPC) Initiative, with Côte d’Ivoire and Guinea reaching the completion point during 2012. This brings the share of countries benefiting from irrevocable debt relief under the HIPC and the Multilateral Debt Relief Initiative (MDRI) to nearly 90 percent of all those eligible. Debt relief provided under the HIPC and MDRI is estimated at US$94.3 billion in end-2011 present value terms. At least one
more country is expected to reach the completion point in the coming months and we continue to work with other eligible countries that could benefit from the initiatives.

As we update our strategy to provide effective TA and training, we will maintain a focus on LICs, even in the face of competing demands from some crisis countries. Highly successful fundraising for capacity building has enabled us to open regional TA and training centers in Kuwait, Mauritius, and, soon, Ghana. We are also bolstering resources at headquarters to maintain backstopping and quality control for TA. For the future, we are adapting our training and technical assistance to make use of new technologies and to respond to demand with new courses such as on job creation and inclusive growth.

IV. BUTTRESSING THE POLICY FRAMEWORK

IMF resources and the global financial safety net

Fund members have responded to the elevated global economic risks by ensuring that the Fund has adequate resources to support member countries. In June, 37 members pledged $456 billion to supplement IMF resources through bilateral borrowing agreements. Together with quota resources and the New Arrangements to Borrow, the new resources, when fully in place, will bring the Fund’s lending power to over $1 trillion.

We must also secure the Fund’s capacity to provide concessional assistance to its poorest members. The recent decision by the Executive Board to use the $2.7 billion in remaining windfall profits from gold sales as part of a framework to put the Poverty Reduction and Growth Trust (PRGT) on a self-sustaining financial basis is an historic step. It is important that all members follow through by committing their shares of the windfall gold profits (which total $3.8 billion) to the PRGT. In this regard, I am very pleased to be able to announce today that I have now received sufficient assurances from members for their support for the PRGT to allow the first distribution of $1.1 billion of reserves linked to windfall gold profits to proceed.

Strengthening Fund facilities

A recent review of the Fund’s facilities for LICs found that the 2009 reforms had succeeded in creating a flexible and streamlined financing architecture, better tailored to members’ diverse needs. Demand for financial and policy support has been high, particularly among the poorer and HIPC-eligible LICs, and demand from small and fragile economies has increased. Staff is working on proposals to further refine and tailor the Fund’s instruments for LIC support, to ensure that the Fund remains able to meet the needs of its LIC members.

The recent Review of Conditionality—building on earlier conditionality reviews and periodic assessments of the crisis programs—found that Fund-supported programs had been tailored to country needs, had adapted to circumstances, and had been built on improved analysis and streamlined conditionality. However, further efforts are needed to strengthen the link between surveillance and program work, including by enhancing risk diagnostics. The Review highlighted the new challenges the Fund faces in ongoing programs, and the need to keep conditionality focused and to improve partnerships with other institutions. While programs had
largely protected priority spending, the social aspects of policy measures in program design also need to be considered in the broader context of employment issues and strategies for inclusive growth.

**Enhancing surveillance**

Further steps have been taken in recent months to enhance IMF surveillance. The new decision on bilateral and multilateral surveillance (the *Integrated Surveillance Decision*) strengthens our legal framework for surveillance. The pilot External Stability Report discussed recently by our Executive Board presents a multilaterally consistent analysis of the external sector for the world’s major economies. In September, the Executive Board endorsed a new Financial Surveillance Strategy to further strengthen financial surveillance in support of global economic and financial stability. These actions position the Fund to address the possible spillover effects from members’ policies on global stability, monitor the stability of members’ external sectors more comprehensively, and engage members constructively on globally important issues. Further work on topics relevant to developing countries include:

- **Strengthening the foundations for our policy advice on capital flows.** The Executive Board has discussed a series of papers on the Fund’s role with respect to cross-border capital flows, managing capital flows, multilateral aspects of policies that affect capital flows, and capital flow liberalization. A fifth paper will synthesize this work and propose an institutional Fund view on the liberalization and management of capital flows. This would not give rise to any new obligations for Fund members, but would provide a consistent basis for Fund advice that is tailored to the circumstances and policy objectives of individual members.

- **To help resource-rich developing countries meet the challenge of transforming resource wealth into support for sustained development, Fund staff has developed new macro-fiscal frameworks and policy analysis tools to enhance our advice in these countries.**

- **We have initiated work to strengthen our analysis of issues involving unemployment, inequality and inclusive growth, including through a surveillance toolkit that will provide practical tools for Fund staff.** Drawing on the expertise of other organizations, macro-social issues that may impact stability will receive more frequent attention in our surveillance.

**V. FUND GOVERNANCE**

The ongoing process of quota and governance reform is essential to the Fund’s legitimacy, and the reforms agreed in 2010 include a doubling of quota resources, a substantial shift in quota shares, and a historic Board Reform Amendment. Significant progress has been made. As of October 10, 134 members with 75.5 percent of quota had consented to their quota increase under the 14th General Review of Quotas. As of the same date, 119 members having 67.6 percent of total voting power have accepted the proposed Board Reform Amendment. Thus, the membership has already achieved both the quota threshold for effectiveness of the quota increases and the required number of acceptances for entry into force of the Board Reform Amendment. However, the membership has not yet met the voting power requirement for entry into force of that amendment, on which the effectiveness of the quota increase also depends.