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-seventh meeting to be held in Washington, D.C., on Saturday, April 20, 2013.
DEVELOPMENT COMMITTEE: THE MANAGING DIRECTOR’S WRITTEN STATEMENT

The global economy has avoided the worst, but it is by no means out of the woods, and prospects may be diverging. Advanced economies need to push ahead with comprehensive plans for fiscal sustainability, while implementing fiscal tightening at a pace the recovery can bear. Activity is picking up in many emerging countries, but they need to be cautious of over-investment and high asset prices. Low-income countries (LICs) are growing strongly, but their slow unwinding of stimulus measures has eroded policy buffers and left them less well prepared to deal with shocks. Commitments are needed from members to implement the agreed funding package that will secure the Fund’s capacity to provide concessional assistance to its poorest members over the long term. The Fund is further enhancing its surveillance, including with a greater focus on risks and spillovers and more coverage of macro-social issues. Energy subsidy reform is a pressing global challenge.

I. ECONOMIC OUTLOOK AND RISKS

World output growth is forecast to reach 3¼ percent in 2013 and 4 percent in 2014. Activity is expected to accelerate only gradually in the advanced economies, as banks are troubled by poor profitability and low capital, while some European sovereigns remain under financial stress. Near-term risks have abated, but important downside risks remain. The main dangers in the euro area are broken credit channels in the periphery and policy adjustment fatigue, with important financial sector reforms still incomplete. Medium-term risks revolve around weak bank balance sheets that inhibit the transmission of low interest rates to the real economy and, in the United States and Japan, the absence of strong medium-term fiscal consolidation plans. Progress in these areas would moderate the spillovers in capital flows to emerging markets from unconventional monetary policy in many advanced economies.

Most emerging and developing countries are again experiencing strong growth, driven by exports and resilient consumer demand. Many of today’s dynamic low-income economies appear to have stronger economic, social and institutional underpinnings of growth than did the previous generation of LICs in the 1960s and 1970s. In the Middle East and North Africa, however, many countries continue to struggle with difficult transitions. In many emerging and developing countries, risks continue to stem from overinvestment and high asset prices.

II. POLICY ISSUES

Macroeconomic Policy Priorities

The advanced economies should support internal demand with continued accommodative monetary policy. Fiscal consolidation should be persistent, but gradual, and the United States and Japan need to design and implement comprehensive medium-term deficit reduction plans. Advanced economies should address weak banks, notably in the euro area, and in some cases provide households and corporate debtors more ways to deal with debt overhang.

Policymakers in emerging markets must not relax their efforts, as some tightening appears appropriate over the medium term. This should begin with monetary policy, supported—as
needed—by prudential measures to rein in excesses in financial sectors. Over time, fiscal balances should return to levels that afford sufficient room for policy maneuver.

The LICs have sustained strong growth—at around 5 percent in 2012. Over half of all LICs remain at least moderately vulnerable to a shock-induced recession, with short-term risks to the global outlook still tilted to the downside. Vulnerabilities stem mainly from the fiscal and external sectors. Many are now less well prepared to manage shocks, as a slow unwinding of stimulus measures has eroded macroeconomic policy buffers; they must balance a need to build reserves and shore up fiscal and external positions against critical infrastructure and social spending needs. Many LICs also need to reform their subsidy regimes to free resources for more productive uses and better insulate their economies from exogenous price volatility.

**International Policy Coordination**

Our Global Policy Agenda (GPA) integrates the Consolidated Multilateral Surveillance Report and the Managing Director’s Action Plan to identify policy issues faced by the membership and to outline how the Fund can assist. The GPA will assess progress across the membership towards implementing policies to put the global economy on a sounder footing, and will assess the Fund’s progress on key elements of its work program. IMF staff continues to provide assessments of individual G-20 members’ progress toward their commitments under the G-20 Mutual Assessment Process. Other recent thematic contributions to the G-20 include an analysis of the main risks to the global economy, a longer-term perspective on imbalances and vulnerabilities within the EMU, and support of the G-20 Data Gaps Initiative.

Recent currency movements have prompted a discussion among Fund members of the cross-country impact of exchange rate policy. The G-20 has reaffirmed its collaborative approach and its members pledge to refrain from competitive devaluation. More broadly, unconventional monetary policy in advanced economies has had mixed effects on others. Early announcements of such policies shored up financial stability in advanced economies and buoyed global asset prices. Later announcements had smaller or more ambiguous effects and may have increased capital flows to emerging markets—especially to those in Asia and Latin America—and some LICs. Prolonged use of unconventional monetary policy could pose risks for financial stability, if it weakens the impetus for needed reforms in advanced economies and encourages excessive risk-taking, misallocation of resources, and sustained large-scale capital flows to emerging markets.

Trade reform is a key tool for durable, inclusive growth, and concluding the Doha Round should remain a priority. Strong efforts are needed to overcome remaining differences. With a recent focus on bilateral, regional, and plurilateral trade negotiations, it is essential that regionalism be transparent, trade-creating, and open. Advanced and major emerging market countries could also expand and simplify trade preferences for the poorest countries and reduce trade-distorting farm subsidies. The rising number of trade restrictions adopted in response to the economic crisis should be reversed and new protectionist pressures resisted. Finally, it is important to ensure the availability of affordable trade finance.
Energy subsidy reform is a global challenge, with 159 economies subsidizing energy; post-tax subsidies are equivalent in total to 2.7 percent of global GDP. The IMF has identified key ingredients for durable subsidy reform, including the need for comprehensive plans, far-reaching communication strategies, phased price increases, improved efficiency of state-owned enterprises, and measures to protect the poor and depoliticize price-setting.

Despite the gradual economic recovery in most of the developed world, donors must fulfill promises to improve aid effectiveness and maintain and expand aid flows. Especially with ODA flows declining relative to other financial flows, the quality of aid and the effectiveness of domestic policies that it can support become paramount. For countries with improved public financial management, the shift toward general budget support should be sustained.

III. FUND SUPPORT FOR A SUSTAINABLE RECOVERY

Demand for financing remains high and the Fund is responding to members’ needs. Flexible Credit Line arrangements for Mexico and Poland were recently renewed and that with Colombia remains in place. Progress is being made in programs with euro area members and the Fund works closely with European partners to address competitiveness, financial market access, balance sheet repair, banking union, debt sustainability, and other challenges.

Fund program engagement includes nearly half of the LIC membership, with an average annual commitment across all LICs of about US$2 billion during 2010-2012. Demand for financial and policy support has been especially high among poorer LICs, and demand from small and fragile economies has increased. The Fund is also assisting the authorities in Myanmar to develop and implement policies, in the context of a Staff-Monitored Program, in order to ensure macroeconomic stability during the transition process.

Progress continues under the Heavily Indebted Poor Countries (HIPC) Initiative, as Comoros reached the HIPC completion point in late 2012. Some 90 percent of eligible countries now benefit from irrevocable debt relief under the HIPC and Multilateral Debt Relief Initiatives (MDRI), with total relief from multilateral and bilateral creditors reaching US$113 billion (end-2011 present value terms). We are working with the remaining four countries that are eligible for the initiatives.

We continue to support the Arab Countries in Transition (ACTs), which face the challenges of maintaining macroeconomic stability and laying a foundation for sustained inclusive growth in a difficult political and economic environment. Three financing arrangements were approved in 2012 for countries in the region, and discussions on IMF arrangements are currently underway with Egypt, Tunisia, and Yemen. We are closely engaged in the ACTs through policy advice and capacity building. 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.

The Fund is maintaining a focus on the effective delivery of technical assistance (TA) and training in LICs. The Africa Training Institute in Mauritius and a new Regional TA Center in Ghana are expected to open in the second half of 2013. We are also updating our strategy to
build on training and TA synergies, for example through a coordinated effort to strengthen monetary policy implementation in Africa. New initiatives include a pilot e-learning module to assist LICs with financial programming and a course on job creation and inclusive growth.

IV. STRENGTHENING THE POLICY FRAMEWORK

IMF Resources and the Global Financial Safety Net

Members have responded to ensure that the Fund has adequate resources to confront global economic risks. To date, 38 members have pledged US$461 billion to be available to the Fund through bilateral borrowing agreements that supplement quotas and the New Arrangements to Borrow (NAB); most of these bilateral agreements are in effect. When fully in place, the pledged resources will bring the Fund’s total potential lending power to over US$1 trillion.

Members are also providing the assurances required to use remaining gold windfall profits as part of a strategy to make the PRGT self-sustaining. We are not yet able to effect the second distribution of SDR 1.75 billion of Fund reserves to the PRGT, however, and encourage members that have yet to provide assurances to pledge to the PRGT their share of both the first and the second distribution of reserves linked to gold sales profits. Pledges of additional loan and subsidy resources are also being sought.

Refining Fund Facilities and Enhancing Crisis Management

A review of the Fund’s facilities for LICs completed in April 2013 found that the 2009 reforms had succeeded in creating a flexible and streamlined financing architecture, better tailored to members’ diverse needs. Our Executive Board approved further refinements that will enhance precautionary financial support to LICs and allow the Fund to respond more quickly when additional financing needs arise during a program. Operational modalities will be streamlined and the flexibility of the Fund’s toolkit for LICs further increased.

A parallel review of PRGT eligibility, also completed in April 2013, concluded that no major changes were needed to the design of the eligibility framework. However, new provisions were introduced for micro states (members with a population below 200,000 people). Marshall Islands, Micronesia, and Tuvalu were added to the PRGT eligibility list on this basis. Armenia and Georgia were found ready to graduate in the 2013 round.

The Fund’s Guidance Note on Conditionality is being revised to incorporate the main findings and recommendations of the 2012 Review of Conditionality, including the recommendation to enhance the macro-social elements of Fund-supported programs. The revised guidance will draw on the recent staff paper on Jobs and Growth: Analytical and Operational Considerations for the Fund and other work.

The first stage of the Review of the Policy on Debt Limits in Fund-Supported Programs, discussed by the Board in March 2013, found that reforms in 2009 were enabling eligible LICs to tap non-concessional resources within a well-specified framework. However, the review suggested further modifications to strengthen safeguards for debt sustainability, while providing LICs increased flexibility to manage their borrowing policy and preserving
incentives for concessional financing. Staff is working on specific policy proposals for further discussion with the Executive Board later in 2013. We are also reviewing Fund policies and practices on sovereign debt restructuring in light of recent experience and will identify issues that could be explored in subsequent staff work.

Enhancing Surveillance

The Fund is undertaking a number of initiatives to enhance surveillance, including by implementing the priorities of the 2011 Triennial Surveillance Review (TSR). The recent Integrated Surveillance Decision allows for a greater focus on interconnections in our surveillance. Our staff reports now have detailed risk assessments—supported, as needed, by risk assessment matrices—and we are implementing the Financial Surveillance Strategy endorsed by the Executive Board. Further work of interest to developing countries includes:

- Spillover reports focusing on the cross-border impact of unconventional monetary policy in advanced economies, including on asset prices and capital flows to emerging markets.
- Recent adoption of a Fund institutional view on the liberalization and management of capital flows, reflected in a guidance note to staff for use in surveillance.
- A new toolkit to enhance surveillance of jobs and growth issues, building on analytical work on job creation, inclusive growth, and income distribution.
- Ongoing work on tools to help inform policy on diversification and structural transformation in LICs in ways that can promote stability and inclusive growth.
- Recent discussion in our Executive Board on the macroeconomic challenges facing small states and how the Fund can engage with them to provide effective advice and support.
- Expanded statistical capacity-building activities, to include working with countries on the measurement of access to banking and other financial services.
- Enhanced frameworks for debt sustainability analysis for members of all income levels, with revamped tools to assess risks to public and external debt.
- Several pilot projects that show promise for further enhancing surveillance:
  - A pilot External Sector Report broadened surveillance for the Euro Area and other large economies, combining a multilateral approach with country detail.
  - New policy tools for resource-rich developing countries were applied to Angola, Azerbaijan, the Democratic Republic of Congo, Iraq, Libya, and Mozambique.
  - We have worked with the World Bank on pilot studies of financial deepening, stability, and macro policy in Benin, Ghana, Haiti, Senegal, and the WAEMU.

V. FUND GOVERNANCE

The 2010 quota and governance reforms—which double quota resources, shift quota shares, and introduce a fully elected Executive Board—will enhance the Fund’s legitimacy and effectiveness. Two of the three steps needed for the reforms to take effect are in place: (i) members representing over 77 percent of total quotas have consented to their quota increase under the 14th General Review of Quotas (70 percent is needed), and (ii) 136 members have accepted the Board Reform Amendment (113 needed). However, the membership still needs to meet the required 85 percent of voting power for adoption of the Board Reform Amendment (71.31 percent reached), on which the effectiveness of the quota increase also depends. The discussion on the Quota Formula Review has provided important
building blocks for agreement on a new quota formula as part of the 15th General Review of Quotas, which is to be completed by January 2014. The 15th General Review will also offer an opportunity to review the adequacy and composition of the Fund’s resources over the medium term, and the distribution of quota shares.