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, Dominique Strauss-Kahn, for the Committee’s eighty-second meeting to be held in Washington, D.C., on Saturday, October 9, 2010.

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DEVELOPMENT COMMITTEE: THE MANAGING DIRECTOR’S WRITTEN STATEMENT

I. Introduction

1. Global economic activity is expanding at a moderate pace, mainly driven by the recovery in emerging Asia and Latin America. Growth in developing countries is accelerating as well, supported by the effects of countercyclical policy responses and growth in demand for commodities. Risks to the global outlook are on the downside, however, with growth in advanced economies expected to remain sluggish.

2. Although the recovery in most emerging and developing countries has come sooner than expected, the crisis has had serious effects on poverty and human development. The recent United Nations Summit on the Millennium Development Goals has underscored the urgent need for the international community to step up efforts to reduce global poverty and make progress towards the MDGs. This requires a renewed sense of shared responsibility amongst advanced, emerging, and developing countries. The advanced economies and leading emerging markets should focus, first and foremost, on securing a strong and sustainable global recovery. They can help ensure that low-income countries share in that recovery by fulfilling their aid commitments and further opening up their markets to these countries’ exports. The developing countries should build on their past successes, mobilizing domestic revenues more effectively to invest in much-needed infrastructure, and rebuild their policy buffers to counter future shocks. The international financial institutions, including the IMF, must also play their part by increasing the effectiveness of their support to developing countries.

3. In this statement, I will first review the economic outlook and key macroeconomic policy issues facing emerging and developing countries. I will then provide an update on the IMF’s role in supporting the recovery, including recent lending reforms and progress in providing debt relief, before moving on to directions for future reform. I will conclude with a review of IMF governance issues.

II. Economic Outlook and Policy Issues

4. Global output growth is expected to increase to 4.8 percent in 2010, and to slow to 4.2 percent in 2011 as the effects of fiscal stimulus programs gradually dissipate. Inflation is projected to stay low, reflecting the still high excess capacity and unemployment rates in advanced economies. The outlook for global economic activity remains subject to downside risks, as concerns about the sustainability of fiscal policies in advanced economies have increased and financial markets continue to be affected by the aftershocks of the crisis.

5. Growth in advanced and some emerging market economies is expected to remain moderate as significant adjustments in household balance sheets, public debt and banking sectors take time to complete. In contrast, emerging and developing countries with good policies have shown resilience during the crisis and many countries have already returned
to higher growth. Countercyclical policy responses and domestic demand growth are contributing to an improved medium-term outlook in a number of countries. As a group, emerging and developing countries are projected to see growth accelerate to 7.1 percent in 2010 and remain high at 6.4 percent in 2011. The outlook varies across regions, however. While growth in emerging Asia and Latin America has been particularly strong and data suggest robust growth also in Sub Saharan African and Middle Eastern economies, the recovery remains more subdued in many parts of emerging Europe and the Commonwealth of Independent States.

6. Macroeconomic policies in emerging and developing economies should remain firmly focused on managing exit from accommodative policies, while fostering medium-term fiscal sustainability and laying the basis for balanced growth. The timing and sequencing of exit from accommodative policies, still in place in many countries, depends on individual country circumstances. In some emerging economies, accelerating inflation or credit growth signal a need for a gradual tightening in monetary policy. While the outlook for inflation remains benign in many other emerging and developing economies, suggesting that monetary policy can remain accommodative, policymakers should be ready to counter inflationary pressures.

7. As regards fiscal policies, in those countries where private demand components are still weak and sufficient policy space is available, policies can remain geared towards supporting activity. In a number of countries, however, significant vulnerabilities suggest a need to focus on fiscal realignment, and all countries facing deteriorated public finances should adopt and publish credible medium-term adjustment plans. While debt remains manageable for most low-income countries, many have seen their debt vulnerabilities increase.

8. Looking forward, rebuilding policy buffers to address vulnerabilities remains a key medium-term challenge for many low-income countries. These buffers, which had been built up as a result of sound policies in the years leading up to the crisis, allowed low-income countries to take unprecedented countercyclical measures when the crisis hit, mitigating its impact. Countries now need to restore future fiscal space over time by strengthening domestic revenues, improving efficiency of spending, borrowing prudently, and advancing structural reforms.

9. The framework of international collaboration has been strengthened in response to the crisis, including through the mutual policy assessments in the context of the G-20 and the work of the Financial Stability Board. To be effective, the efforts to secure the global recovery and implement the reforms needed to prevent future crises must continue to be cooperative. Collective efforts are also called for to ensure that the Gleneagles promises on aid are kept, allowing developing countries to finance urgent infrastructure needs and respond to the challenges of climate change. And new impetus is needed on global trade reforms that have the potential to unleash new sources of productivity and growth in developing countries. Opening up trade is one of the most important ways that advanced countries can further help their low-income neighbors, and without budgetary costs.
Concluding the Doha Round should be a priority, but we need not wait for that: advanced and major emerging market countries could act now by expanding and simplifying trade preferences, shifting them in favor of the poorest, and tackling trade-distorting agricultural subsidies.\(^1\)

### III. Enhanced Support during the Crisis and Recovery

10. The IMF responded quickly to the global economic crisis with record-breaking levels of financial assistance to its members, while overhauling its general lending framework and streamlining conditions. Since the beginning of the crisis, the IMF has provided emerging and developing countries with about US$186 billion in financial support, of which US$6 billion in concessional resources to low-income countries. This support has eased liquidity constraints and catalyzed donor support, helping countries to implement countercyclical policies and preserve critical social spending. In addition to lending, the general allocation of Special Drawing Rights (SDRs) totaling US$250 billion allowed many developing countries to build up their depleted international reserves without having to divert resources from essential public spending.

11. Precautionary arrangements, such as the Flexible Credit Line (FCL) and the High Access Precautionary Stand-by Arrangements (HAPAs) have helped stabilize emerging economies and mitigate potential contagion effects. The IMF has recently adopted two further important reforms to its toolkit for crisis prevention in emerging economies: we introduced a new Precautionary Credit Line (PCL) for members with sound economic policies and only moderate vulnerabilities, and the FCL was improved to allow for more flexible access for a longer period of time. The rigorous qualification processes for these credit lines, with conditionality in the PCL focusing on remaining vulnerabilities, will broaden the availability of insurance instruments to our members while protecting resources and limiting the risk of moral hazard.

12. We also remain firmly committed to assisting low-income countries in facing the uncertainties of the global economic environment. We have reformed our lending facilities for low-income countries, significantly increased our medium-term concessional lending capacity, and eliminated interest charges on all concessional IMF lending until 2012. In addition to these reforms, we have established a new Post-Catastrophe Debt Relief (PCDR) Trust that allows the IMF to join international debt relief efforts for very poor countries that are hit by the most catastrophic of natural disasters. PCDR Trust debt relief can free up additional resources to meet exceptional balance of payments needs created by catastrophes and to aid the subsequent economic recovery efforts. In July 2010, the new Trust was used to provide full debt relief to Haiti, the equivalent of US$268 million, following the devastating earthquake in January.

\(^1\) For a detailed discussion of these issues, see: *Reaching the MDGs: An Action Plan for Trade*, IMF Staff Position Note 10/14 (available at www.imf.org).
13. Significant progress continues to be made in reducing the debt burden of low-income countries under the HIPC Initiative and MDRI. Since the Spring Meetings, two countries (the Democratic Republic of Congo and Liberia) reached the completion point and received irrevocable debt relief. Moreover, Comoros reached the decision point and began to receive interim relief. All in all, 30 of the 40 HIPCs have reached the completion point and 36 have reached the decision point.

14. A number of low-income countries with IMF-supported programs have begun to take advantage of our new policy on debt limits. The new policy is designed to provide more flexibility for borrowing strategies, and is based on an assessment of the risk to debt sustainability and of the authorities’ capacity to manage public resources, providing space for some non-concessional borrowing to finance public spending, including key infrastructure investments.

IV. Directions for Further Reform

15. Thanks to significant reforms to lending arrangements and an increase in resources, the IMF is well-positioned to support its members during the recovery. However, work continues on further improving the ability of the Fund to respond to future crises in three key areas:

- *First, we are modernizing the framework and modalities of surveillance.* This includes more attention to multilateral analysis; greater value and traction from bilateral surveillance; enhanced financial sector analysis; and better integration among all dimensions of surveillance. The IMF is working on new modalities for integrating spillover analysis on a trial basis for systemic economies in order to provide more candid assessment and debate of the global effects of domestic policies. We have also adopted a more risk-based approach to financial sector surveillance which will integrate financial stability assessments conducted under the Financial Sector Assessment Program into Article IV surveillance for countries with systemically-important financial centers. The multilateral perspectives in cross-country/thematic Article IV reports and greater flexibility in determining the Article IV consultation cycles will help us to enhance the relevance and quality of bilateral surveillance. A joint IMF-FSB G-20 initiative is addressing data gaps in support of more effective financial sector and multilateral surveillance.

- *Second, we are considering new ways to provide more coordinated financial support in times of crisis.* Options under discussion include multi-country arrangements, enhanced cooperation with regional financing arrangements, and the possible establishment of a Global Stabilization Mechanism that could be activated in the event of a systemic crisis.

- *Third, there is a need to do more to strengthen the long-term stability of the international monetary system.* Persistent global imbalances, unprecedented accumulation of international reserves concentrated in a few currencies, and volatile
capital flows and exchange rates represent complex long-term problems. These interrelated issues arise against the background of uncertain access to international liquidity in times of crisis. They also partly reflect transition challenges, with emerging markets growing much faster than advanced economies—often with export-led growth strategies—and yet having relatively underdeveloped financial markets. Pragmatic responses to these problems could include finding alternatives to self-insurance, adopting a multilateral approach to reducing capital flow volatility, and diversifying the supply of reserve assets. The latter could possibly be facilitated by encouraging greater use of the SDR as an alternative reserve asset.

16. The IMF, working with other development partners, will continue its efforts to help low-income countries meet their key challenges:

- **Mindful of the large infrastructure investment needs, the IMF is helping low-income countries strengthen domestic revenue performance, boost their capacity to make productive investments, and borrow safely.** In this context, the IMF and the World Bank are working on tools to help countries assess their capacity to manage public investment. The IMF is also helping to build capacity in low-income countries to handle the macroeconomic management of aid inflows, debt management, public financial management, tax policy and administration, and the fiscal challenges faced by natural resource-rich economies. With the help from donors, the IMF is strengthening its network of regional technical assistance centers, particularly in Africa and Central Asia.

- **We are working with countries to rebuild the macroeconomic policy buffers which served them well during the crisis.** To improve our analysis of low-income country vulnerabilities, we are developing a new “vulnerability exercise” for low-income countries to parallel the efforts made in recent years for advanced and emerging market economies. At the same time, the international community needs to help low-income countries make their economies more resilient to shocks. In this regard, several policy options should be considered, including a deepening of domestic financial systems, the introduction or expansion of well-targeted social safety nets, contingent repayment terms on official borrowing, and the development of markets for special instruments such as terms-of-trade indexed debt.

- **Finally, we are launching a review of our engagement in fragile countries.** In light of the particular macroeconomic challenges in these countries, we are considering how the IMF can improve its effectiveness—in close collaboration with other partners—in providing technical, policy and financial support.

17. Our efforts in support of low-income countries need to be backed up by sufficient resources. In the context of the recent reform of lending facilities for low-income countries, the IMF’s members agreed to raise loan and subsidy contributions for the Poverty Reduction and Growth Trust (PRGT) to provide up to US$17 billion to low-income
countries in the period through 2014. Several members have made pledges to this effect, but additional commitments are still needed to meet this goal.

V. Fund Governance

18. The IMF’s membership is committed to completing further quota reforms before January 2011. These reforms should lead to a substantial increase in the voting power of dynamic emerging market and developing countries, while protecting the voice of the poorest members. The appropriate size of the IMF’s quota resources is also being considered as part of this review. Over the years, the IMF’s quota resources have not kept pace with the expansion in global trade and financial flows. A significant increase in quotas is desirable, to give confidence that resources are available to tackle the worst-case scenarios, and to preserve the quota-based nature of the IMF. Other aspects of the IMF’s governance are also under review, including the composition of the Executive Board, ministerial engagement, the leadership selection process, and staff diversity.