Statement by the Honorable José De Gregorio
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The world economy is growing unevenly and is subject to many tensions. Most advanced economies (AE) are still recovering from the crisis and have weak fiscal positions. In contrast, emerging market economies (EM) have been growing strongly and some of them face the need to prevent overheating. At a global level, the buoyancy of EMs has contributed to higher commodity prices. This poses significant challenges to the membership and also to the IMF. How to keep bilateral and multilateral surveillance relevant under current circumstances, and how to ensure a well-functioning International Monetary System (IMS) going forward are key issues we currently face.

I. Global Rebalancing: Policy Challenges

High commodity prices and risks of overheating in some parts of the world suggest that the recovery phase has ended in several economies. Although growth remains markedly uneven, and thus appropriate policies differ according to country circumstances, there is a case for further moderation of the fiscal stance. In those AEs with high public debt burdens, short-term negative effects of fiscal consolidation on aggregate demand might be inevitable, but the trade-off between short-term gain and long-term pain will become increasingly unpalatable. In other economies where high growth and inflation are testing macroeconomic stabilization, a shift towards a more neutral fiscal stance should lessen the burden on monetary policy, and mitigate the risk of policy inconsistencies. However, given the rigidities in fiscal policy implementation, monetary policy adjustments geared towards price stability and sustainable growth should not be delayed.

More debated tools are intervention in the foreign exchange market and the use of capital account policies. Regarding the former, its monetary effects should be sterilized, so as to shield the conduct of monetary policy, and should not limit real exchange rate adjustments in accordance with fundamentals. Economies with risks of internal overheating and structural surpluses in external accounts should allow their real exchange rate to appreciate as part of the adjustment.

Regarding capital account policies, they can play both a macroeconomic role, if they succeed in reducing current account deficits and buoyant domestic demand, and a macro-prudential role, if they help avoid the build-up of financial vulnerabilities. However, their actual effectiveness in these areas is still a matter of debate. Apart from limitations to their effectiveness, capital controls bring about clear distortions, such as redirecting capital inflows from regulated segments of the financial system to unregulated ones, fostering the shadow banking system, and increasing market segmentation in terms of access to finance across households and firms.

II. Implications for Surveillance

Current global developments have a bearing for the Fund's approach to multilateral surveillance. Too often we see the divisive discussion on current accounts and real exchange rates take center stage in our debate. We should acknowledge that these are the results of saving and investment dynamics across economies, the true underlying forces driving global rebalancing. We encourage the Fund to include these trends in multilateral surveillance, for instance, by institutionalizing the monitoring of the indicators that it already provides in the context of the Mutual Assessment Process (MAP).

Regarding capital account policies, we remain skeptical that eventual surveillance principles can have useful traction now. First, domestic financial systems are widely heterogeneous across countries. Cross-country portfolio shifts can occur through channels, such as cross-border derivative contracts, where our knowledge is still limited. Second, the dividing line between capital account policies and macro-prudential tools is blurred, and it is not obvious that precise guidelines can be usefully applied to this whole range of instruments. Third, history shows that financial integration has proceeded apace, in spite of short-term turmoil, without specific guidance or a structured multilateral process. The benefits of financial integration are strong enough that members will continue to embrace it, at a pace that has been, and will continue to be, dependent on country circumstances.

We encourage the Fund to focus its efforts on understanding the actual implications, spillover effects, and distortions brought about by capital account and macroprudential measures. This would go a long way to prevent the collective action problem that arises from policies that spill across borders through financial interlinkages. If all countries apply policies which, at the margin, keep net capital flows constant, global adjustment will be impaired. At a later stage, when sufficient knowledge has been accumulated, the Fund can refine the rules of the game for policies that have cross-border financial implications. Thus, we welcome the preparation of spillover reports on an experimental basis under the Article IV Consultations for the five major economies.

III. The International Monetary System (IMS)

The financial crisis in core advanced economies led to a significant monetary expansion and a weakening of fiscal positions, putting pressure on the IMS in two related ways. The first is that while the supply of reserve currencies is mostly driven by country-specific circumstances, limited convertibility and flexibility prevail in several large dynamic economies. The second is related to the uncertainties on whether the IMS can provide for an adequate safety net to confront future international financial instability.

The Fund is well placed to promote adequate collaboration between the main economic zones to face these challenges successfully. Insofar as furthering the role and changing the composition of the Special Drawing Rights (SDR), or the formalization of liquidity provision arrangements, do not replace realistic global policy coordination and dialogue, these initiatives should be welcomed.

IV. IMF Financing and Governance

After the approval of the quota and governance reform package late last year, we support the timeline for implementation by the 2012 Annual Meetings. We welcome the activation of the New Arrangements to Borrow (NAB).

We look forward to working with the new IMFC Chair towards increasing the effectiveness of the IMFC. Key elements in this path are to enhance the engagement of capitals in the IMFC process and strengthening the spirit of compromise. Macroeconomic and financial issues might become less pressing in the global political agenda over time, but the IMFC cannot lose sight of their importance. Practical steps that could be adopted are the exploration of synergies between multilateral processes such as the MAP and IMF spillover reports; increasing the number of joint G-20/IMFC activities, including restricted sessions; and scheduling the Deputies activities close to the date of IMFC meeting.

Finally, we would like to reiterate our support for the selection of Management under a transparent, open and merit-based process.