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IMFC Statement by Taro Aso
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Statement by the Honorable Taro Aso
Deputy Prime Minister of Japan and Governor of the IMF for Japan
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I. THE GLOBAL ECONOMY AND THE JAPANESE ECONOMY

Global Economy

The global economy continues to present steady growth. Growth is projected to continue, although the growth momentum is moderating. However, growth prospects vary from country to country, with peaks in 2018 in some advanced economies. Also, risks are skewed to the downside and some risks have already materialized. Especially, capital outflow from emerging market economies and trade tensions are the main downside risks.

As the global capital market conditions tighten while monetary policy normalizes in some advanced economies, a reversal of capital flows into emerging market economies is occurring. So far the phenomenon remains idiosyncratic to each individual country, but similar risks are mounting in emerging market economies with vulnerable economic situation such as persistent large current account or fiscal deficits. Although the negative impacts have not spread throughout the global economy, we should be more vigilant and move fast so that the international community can provide assistance when needed.

Trade tensions remain high. Trade conflicts aggravate market sentiment, increase financial vulnerabilities and discourage investments. Heightened trade barriers would adversely affect global supply chains, stagnating production and investment throughout the world. Inward-looking policies with protectionist measures would not benefit any country. Unilateral and protectionist trade measures could trigger tit-for-tat retaliations, shrinking world trade transactions in a short period of time. It is critical to accelerate global economic growth through free, fair, and rules-based trade, and we should purse solutions through multilateral, rather than bilateral, frameworks to that end.

To deal with these downside risks, the commitment to use monetary, fiscal and structural policies both individually and collectively continues to carry significance. In order to prepare for the future while the economic conditions are still favorable, we should rebuild fiscal buffers as necessary to create room for investment in high quality infrastructure and human capitals, and to ensure the debt-to-GDP ratio to be on a sustainable path. Policy responses to structural problems such as aging and decline of productivity are also essential.

Japanese Economy

Japan's economic fundamentals are solid as Abenomics has been making steady progress: real GDP has been growing for three consecutive years; private demand-led growth is robust mainly by growing private consumption and capital investment; labor market remains tight, and the unemployment rate is 2.4 percent in August marking the lowest level in about 25 years; and wage is increasing at a high rate of about two percent in five consecutive years.

From the medium- to long-term perspective, Japan's biggest challenge is aging population with declining birthrate. As Japan is in a dire fiscal situation with its central and local government debt level reaching twice as large as its GDP, restraining increases in social security expenditure is an unavoidable challenge. Against this background, we set out a new fiscal reform plan in June, aiming for fiscal consolidation, and setting the target of achieving primary surplus by FY2025. As the baby boomers will have turned 75 years old or above by 2025, social security spending is expected to surge. We therefore need to solidify the path to fiscal consolidation in time. Through steady implementation of expenditure reforms according to the plan, we will ensure that we achieve the goal.

Regarding the consumption tax rate increase to ten percent planned in October 2019, the additional revenue will be spent in a well-balanced manner for both investment in child-caring generations and stabilization of social security. We expect this would go all the way to lessen anxiety of working generation and to encourage consumption, in addition to fiscal consolidation. We continue our efforts to realize an economic environment that would ensure the consumption tax rate hike as planned in October 2019.

II. EXPECTATIONS FOR THE IMF

It is important to strengthen the function of the international financial architecture, which helps the IMF member countries eliminate their vulnerabilities. We highly value the IMF's long-standing efforts to enhance its surveillance capability and make full use of it to monitor the global economy, provide countries in need with swift loans, and boost economic growth through capacity development. The prompt agreement of the SBA for Argentina facing severe difficulties has impressed the international society once again with the IMF's role in preserving stability of the global economy. Japan will assume the G20 Presidency next year, and we are determined to play a leading role in achieving strong, sustainable, balanced, and inclusive growth of the global economy. We expect the IMF's continued contribution in analyzing and addressing challenges that the global economy faces.

Surveillance

Excessive Global Imbalances:
Excessive global imbalances pose a risk to the global economy. Given that the current account balance of each country reflects its macroeconomic saving-investment balance, each country should carry out

appropriate macroeconomic and structural policies to achieve a sustainable saving-investment balance, thereby endeavoring to help eliminate excessive global imbalances. If we treated this issue in the context of bilateral trade and tried to address it by imposing tariffs, it would not resolve global imbalances. It is essential to address this issue in a multilateral framework, and it is critically important for the IMF's surveillance to provide a common level playing field.

In this regard, the External Balance Assessment (EBA) model and the External Sector Report are useful as tools to assess countries' external positions in a transparent and even-handed manner. We highly value the IMF's work in reviewing the EBA model to more precisely capture demographic changes and generational differences in saving behavior. On the other hand, fundamental questions still remain. Although the model's assessments of real exchange rates based on current account balance analyses tend to attract much attention, such assessments linking exchange rates to current account balances are no longer valid for many countries. For example, income balance, on which exchange rate does not function well as an adjustment mechanism, now occupies significant share in the current account balance in growing number of countries, particularly in advanced economies. In addition, capital transactions, which are conducted quite independent of current account transactions, have significantly increased in size and come to play a dominant role in determining exchange rates. We believe that the IMF should use the EBA in line with its original motivation to identify excessive imbalances by analyzing the current account balance and to propose structural reforms to address them, instead of focusing too much on assessing exchange rates in reference to current account balances.

Capital flows:
Now that rapid reversals of capital flows are observed in some emerging economies, policy responses to such capital flow reversals are important in both capital exporting and importing countries. The lesson that the international society learned from the Asian Financial Crisis 20 years ago is that certain capital flow management measures (CFMs) are appropriate and necessary. Japan highly values the IMF's Institutional View on capital flows (IV) which indicates that CFMs can be allowed under certain circumstances. The IV has moved to a phase to be tested its usefulness in practice. The IMF should assess each country's CFMs, taking into accounts individual countries' specific circumstances, in an even-handed and ex-post verifiable manner. We welcome that the IMF has compiled the cases of actual applications of the IV. We encourage the IMF to continue the compilation further as it would provide a helpful guidance for policymakers.

Aging population and declining birthrate:
Rapid aging of population and decline in birthrates are observed not only in advanced countries but also in some emerging and developing countries. By 2050, the world population over sixty years old is projected to reach two billion. Aging population and declining birthrate would require policy responses not just to mitigate the trend itself, but also in wide-ranging areas such as reduction in the labor force, intergenerational equity, and financial inclusion. To provide a common basis for countries to discuss these issues, we expect the IMF to analyze the effects of population aging and declining birthrate on macro economy, fiscal conditions, and finance.

Support for Low-Income Countries

The last few years have witnessed rapid debt build-up in some developing countries stemming from debts owed to non-traditional creditors and non-concessional borrowings. Both borrowing countries and creditors, public and private, have a shared responsibility to work on this issue to enhance debt transparency and ensure debt sustainability.

In this regard, ensuring debt sustainability through enhanced debt transparency would eventually lead to steady investment inflows to developing countries, thereby serving them as a solid basis for their economic growth. To this end, countries need to disclose accurate data on their debt, but the lack of capacity of these countries is profound. IMF's role will be crucial in identifying their capacity gap and providing effective assistance to them within a reasonable time frame in an appropriately sequenced manner. We welcome the IMF's multi-pronged approach, which includes the provision of technical assistance to enhance debt transparency and ensure debt sustainability, and expect its steady implementation. Specifically, we expect the IMF to strengthen their technical assistance further, so as to help improve quality of debt statistics and to help implement the refined Debt Sustainability Framework for Low-Income Countries. Japan intends to actively cooperate with the IMF on these efforts. We also expect that the IMF's Debt Limit Policy and conditionality of IMF-supported programs will be reviewed in such a way as to enhance debt transparency and ensure debt sustainability.

In addition, it is crucial to build capacity in domestic resource mobilization (DRM) and public financial management to ensure debt sustainability. In this regard, we call on the IMF to further support development and implementation of medium-term revenue strategies, which are key to DRM, in more countries. Moreover, in order to maximize the impact of assistance in DRM, coordination among IMF technical assistance projects, including the Tax Administration Diagnostic Assessment Tool, and collaboration among development partners are important. We expect the IMF to strengthen collaboration with the other partners through the Platform for Collaboration on Tax, and continue to provide regular updates on its activities.

Not only borrowers but also creditors should work to enhance debt transparency and ensure debt sustainability. In this regard, emerging and private creditors should fully recognize the importance of sustainable financing practices. We expect the IMF to actively reach out to such creditors to promote their understanding so that sound sustainable financing practices will be embedded in their lending activities.

Capacity Development

The IMF's capacity development (CD) activities are playing greater roles and increasing their importance, given the huge demands that still remain especially in low-income countries. Japan has been actively supporting the IMF's CD activities and commits to engaging further in areas in which enhanced activities are warranted. We appreciate the IMF's efforts to advance outcome-oriented evaluation on and enhance effectivenss of its CD activities through the Result-Based Management (RBM) framework in the current circumstance where the IMF increasingly relies on external financing for its CD activities. In this regard, we encourage the IMF to indicate to us specific examples and effectiveness of the RBM framework at the IMF's CD Strategy Review scheduled later in this year. Moreover, in order to utilize the limited resources of the CD activities effectively, it is essential to further enhance collaboration among the IMF departments to better understand the CD needs across all regions and to deliver CD supports in a geographically-balanced manner.

Global Financial Safety Net

In overcoming the Global Financial Crises, the global financial safety net (GFSN) has been strengthened in the multi-layered structure composed of foreign reserves as the unilateral layer, bilateral swap arrangements as the bilateral layer, regional financing arrangements (RFAs) as the regional layer, and the IMF as the global layer. These layers of the safety net function individually and collaboratively to improve the stability of the current international financial system in both crisis prevention and resolution. As an excellent example, we highly value the joint test-runs that the IMF has conducted with the Chiang Mai Initiative Multilateralization (CMIM) based on realistic assumptions.

In this sense, it is highly significant that the IMF is adequately resourced. While the 15th General Review of Quotas is aimed to be concluded by the Spring Meetings of 2019 and no later than the Annual Meetings of 2019, however, views remain greatly diverged among member countries on such core elements as the size of the Fund, the modality to strengthen it, and a quota formula. We should continue our discussions tenaciously at the IMF to reach consensus.

As a possible way forward, Japan emphasizes the usefulness and importance of borrowed resources as the IMF's resource. The 14th General Review of Quotas which was agreed in 2010 in the middle of the Global Financial Crisis came into effect in 2016, which was a great progress since it doubled the total amount of quotas. At the same time, Japan took the lead to offer contribution of 100 billion dollars to the IMF, which gave great assurance to the markets and strengthen the Fund's resource. Bilateral loans from other countries followed, subsequently incorporated into the New Arrangements to Borrow (NAB) in 2011. Later, as the European debt crisis became severer, another bilateral borrowing arrangements were agreed. These experiences show that the NAB and bilateral borrowings have played essential roles for the IMF to secure necessary resources in a timely manner. In the current environment where the global economy faces downside risks and some emerging market economies are in dire predicaments, borrowed resources would play a similar role effectively should the IMF face an urgent need for resources.

Contributions from the member countries are essential also for the Poverty Reduction and Growth Trust (PRGT) which is a central framework for lending to LICs. Japan has contributed cumulatively the largest amount among member countries, accounting for approximately 25 percent of the total PRGT loan funding and approximately 13 percent of the interest subsidy. A mechanism to provide a proper incentive for member countries to make financial contributions is essential for the IMF to operate smoothly and reliably, and to improve the stability of the GFSN. As one of such possible mechanisms, the element of "voluntary financial contribution (VFC)" should be reflected more prominently in the quota formula, thereby strengthening the incentive for members to contribute to further enhancements of the IMF's resources.

Emerging issues:

We are witnessing rapidly progressing technological innovation. Particularly in the financial sector, it is bringing about considerable changes which urge financial institutions to transform their business models. We need to utilize such development to support economic growth, while mitigating its potential risks.

For example, risks are recognized that virtual currencies and crypto-assets might pose for money laundering and tax evasion, and to investor protection and market integrity. Considering their cross-border and cross-sectoral nature, relevant authorities should cooperate to properly manage such risks. On the other hand, the underlying technologies such as distributed ledger technology could be useful. It is therefore important to ensure a conducive environment to promote, without overkilling, progress of technological innovation.

We welcome the Bali Fintech Agenda, which captures both risks and opportunities of fintech in a balanced manner. We expect that IMF will deepen its consideration on fintech in light of this Agenda.