# International Monetary and Financial Committee

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**IMFC Statement by Wolfgang Schäuble**
**Federal Minister of Finance, Germany**

On behalf of Germany

# Statement by Mr. Wolfgang Schäuble
# Minister of Finance of the Federal Republic of Germany
# to the International Monetary and Financial Committee
# Washington, 16 April 2016

## I. Global Economy and Financial Markets

### Global Economy and Euro Area

Global growth is expected to increase in 2016 and 2017 but remains moderate and uneven across regions and countries. Emerging markets and developing economies are still growing stronger than advanced economies, however in 2015 and 2016 at a lower speed than in 2014. This slowdown is related to the necessary ongoing transition of the Chinese economy, to lower commodity prices, to earlier exaggerations and domestic shortcomings in some countries, like insufficient structural reforms. Downside risks for the global economy have increased since October 2015, in particular due to geopolitical tensions. It is to be noted that many emerging market economies are better prepared to weather challenges compared to earlier decades, in particular because of higher buffers and more widespread flexible exchange rate regimes. Strong domestic policy action, tailored to the specific needs and circumstances of individual countries, will increase each countries' resilience and thus ensure that increased risks do not endanger the current growth path, but underpin it and make it stronger.

Repeated downward revisions of global growth over the last years highlight that structural factors are at play. While monetary policy can usually influence the rate of utilization of the production potential, it alone cannot ensure sustainable growth. Monetary policy is no substitute for sound and sustainable fiscal policy and structural reforms. Still too high private and public debt and a lack of investor and consumer confidence are important obstacles to a more dynamic global economy.

The limitations and negative side-effects of expansionary macroeconomic policies become more visible, the longer they are applied. They could facilitate complacency as regards fiscal, financial and structural reform needs. The number of advanced economies that tightened their fiscal stance has decreased remarkably over the last years. Notably, countries that failed to address structural rigidities and are burdened with high public debt and deficits are facing problems to recover. Over the last decades, the trend of ever-increasing public debt ratios of advanced economies went hand in hand with a trend of lower structural growth.

Against this background it is particularly worrisome that the ambition for growth-enhancing structural reforms appears to have slowed down in many countries. G20 members have committed to an impressive list of broad-based structural reforms. These reforms have to be implemented rigorously. Together with sound fiscal policies to strengthen the sustainability of public finances and making the composition of public expenditure and taxes more growth-friendly, this is the best way to increase the dynamism and resilience of the global economy.

In the euro area, the economic recovery is continuing, despite global risks: real GDP growth has been positive for eleven quarters in a row and annual growth is expected at 1.7% this year. At the same time, budget consolidation efforts undertaken over the last couple of years have led to visible results, including a decline in the euro area aggregate debt ratio. However, more recently, efforts to consolidate public finances have lost momentum. Unit labor costs and current account balances have improved substantially, and unemployment rates have been on a downward trend since mid-2013. At the current stage it is essential to focus efforts on both: raising potential growth through structural reforms and reducing public debt through growth-friendly fiscal consolidation and adherence to EU fiscal rules.

The European sovereign debt crisis has shown, that in a monetary union, loss of confidence can have dramatic effects. The developments in recent years drove home the point that public finances in the European Monetary Union need to live up to especially high standards. Loosening fiscal policy would not help the euro area to return to stronger growth in the long run, as several Member States still face substantial public deficits and high debt ratios. The combination of structural reforms and growth-friendly consolidation will strengthen confidence, foster employment, and increase the euro area’s long-term growth perspectives.

**Germany**

By maintaining continuity and reliability, German fiscal policy contributes to the upswing in the German economy and to stability in Europe. The German government expects the economy to grow by 1.7% in real terms in 2016. Domestic demand, in particular consumption of private households, continues to be an important driver of economic growth. Record employment and associated increases in income, as well as low interest rates and stable prices, are key factors in this regard. However, with a view to a normalization of interest rates and the longer term perspectives associated with an ageing population, challenges to sustainability cannot be ignored.

Germany’s growth-friendly fiscal policy continues to complement and support the favorable economic situation. The general government budget has been close to balance for four years in a row. Germany will stay on the path of sound public finances and stick to its balanced budget. Mastering the refugee situation remains the top priority. For this reason, the federal government has just allocated a further amount of about 10 bn. euros to address this challenge in 2017. It shows how important sound fiscal policies are to maintain a government’s capacity to act. However, given the higher degree of uncertainty in the global economy and taking into account the extraordinary circumstances in financial markets, fiscal policies need a high degree of caution and expenditure control.

Consolidation has also opened up leeway for tax relief and investment: Until 2019 the German government will increase measures to raise public investment by an average of 4% per year to target areas like research and development, infrastructure and education, which are crucial for fostering long-term growth. Due to growth in public investment, tax relief for low and middle income earners, families and single parents, increasing public expenditures on social security and significant additional expenditures associated with the influx of refugees, and given the cyclical position of the German economy, fiscal policy in 2016 is already considerably expansionary.

**Financial Sector**

The balance between economic and financial risk taking has to be watched closely. Risks to global financial stability have recently emanated from emerging market economies, as concerns about growth prospects have led to increased spillovers to global financial markets. Market corrections may have been amplified by structural changes in market liquidity. Attentiveness is warranted and it is only reasonable to assume that further corrections might eventually take place. This could lead to considerable losses for market participants and may have broader effects on the real economy. In some advanced economies, there is an increasing concern that the growth outlook continues to deteriorate. The efficacy of extraordinary policies and ultra-low interest rates is being called into question and we need to pay close attention to negative side effects on financial stability. Notably the less well-regulated segments of the financial sector may be an additional source of vulnerability and deserve heightened scrutiny. Overall, the current financial market environment poses an increasingly important challenge for policymakers and we will remain alert with regard to any emerging risk.

After the financial crisis in 2008, we have made important progress to build a stronger and more resilient financial system. In particular, though certainly not exclusively, we have improved the soundness of the banking sector. However, our job is not finished. Going forward, priorities are to continue to reduce risks within the banking sector; this includes addressing the “too-big-to-fail”-problem by making sure that bail-in provisions are credible and implemented consistently, including by ensuring adequate levels of additional loss absorbing capacity of systemically important institutions. In the current low interest rate environment, the development of mortgage markets needs to be monitored continuously. Furthermore, we need to advance our efforts to appropriately monitor and supervise the shadow banking sector. Reforming the over the counter (OTC) derivatives market will help to reduce systemic risk and increase transparency. Full and consistent implementation of internationally agreed reforms will be crucial to further strengthen the financial system. Beyond that, further steps have to be taken to ensure that financial stability is set on firmer ground. In this regard, we see merit in further exploring links between financial institutions and sovereigns and possible implications.

In the euro area, the Banking Union is making good progress: at the end of 2014, the Single Supervisory Mechanism was put in place and the ECB has assumed responsibility for supervising the largest banks in the euro area. At the beginning of 2016, the Single Supervisory Mechanism was complemented by a Single Resolution Mechanism for banks. The Single Resolution Board has begun its work and the European bail-in rules are fully in force, ensuring that shareholders and creditors will have to bear the resolution costs in the first place, which reduces moral hazard and is an important step away from bail-outs paid by taxpayers. It is now a priority to ensure (i) that the agreed rules and regulations are credible in practice and (ii) that risk potential for the banking sector is rigorously reduced. To this end, credible levels of loss absorbing capacity have to be available in banks, while regulation has to reduce the sovereign-bank nexus and, in particular, the concentration of domestic sovereign debt in bank balance sheets. Banks must reshape their business models to enhance profitability in an environment of low interest rates and digital change. Besides, the Single Supervisory Mechanism as well as some member states have to address crisis legacy issues and elevated NPL levels, in line with European competition rules and market principles, while reducing excess capacity in the euro area banking system over time. Further mutualization of bank risks, for example by introducing a common European deposit guarantee scheme, should not be considered. What we need now are additional structural measures to substantially and sustainably reduce these risks and clean up bank balance sheets.

**International tax system/ BEPS**

It is highly important to develop a fair and modern international tax system. Therefore the international consensus on the BEPS (Base Erosion and Profit Shifting) recommendations is a tremendous success. Such international coordination is the only way to prevent BEPS effectively. For this reason, the continued fight against BEPS will remain on top of the international tax agenda, now that the BEPS project has entered the implementation phase. The inclusive framework that was recently welcomed by the G20 Finance Ministers will monitor further progress, while ensuring that all interested countries and jurisdictions can participate on an equal footing, making it a truly global initiative. Germany will continue to play an active part in this process and promote further international cooperation in tax matters. Germany values the work of the IMF on international tax issues.

The recent release of data ("Panama Papers") shows that progress in the area of tax transparency still needs to be made. We should not allow the beneficial owners of legal arrangements to hide from tax administrations and other law enforcement agencies. The G20 should reaffirm the need for the countries of relevance to endorse and to properly implement the Common Reporting Standard (CRS) without further delay. To speed up the implementation process and to increase pressure, the G20 should mandate the Global Forum to develop a mechanism for sanctions for non-compliant jurisdictions.

## II. International Financial Architecture and IMF Policies

### IMF Quotas and Governance

We welcome the implementation of the 2010 reforms, which is of great importance for the Fund's credibility, effectiveness and legitimacy. With the quota increase the Fund's character as a cooperative quota-based institution has been strengthened and its own resources have been augmented to a comfortable level.

We look forward to the upcoming discussions on the 15th General Review of Quotas. For a successful and timely outcome, we deem the appropriate sequencing of discussing its elements crucial. Given its decisive role for an agreement, we will first need to agree on the adequate size of the Fund in terms of quotas and any respective need to increase quotas. In a second step and on this basis, a fruitful discussion on the quota formula and the ensuing possible quota shift to countries that are underrepresented with a view to their position in the world economy can follow.

Germany continues to stand ready to constructively discuss all elements of the review. This includes the quota formula, which should continue to adequately reflect the unique role and mandate of the Fund and has to take into account the interests of all member countries. We reiterate our opinion that these discussions form an integrated package, and that no decisions are to be taken in isolation.

### The international monetary system and the global financial safety net architecture

The international monetary system and the architecture of the global financial safety net (GFSN) are key topics for this year's Spring Meetings. The IMF has made important contributions to these debates, and we look forward to further reviewing the adequacy of the GFSN as well as to the Fund's forthcoming analysis of capital flows and country experiences in dealing with surges and sudden stops.

The current GFSN architecture has been strengthened on several fronts in recent years, leaving it well-equipped to deal with shocks and to provide assurances for countries. The global safety net has evolved into a more diverse and multi-layered system with the IMF at its core, increased reserves on the national level, and other elements designed to meet specific demands at the regional or bilateral level. We view this development as a distinct source of strength, which should not be put in doubt. It enables a flexible, tailored approach to assist countries in times of crises, and it reflects the diversity of the international monetary system as well as the mandates of the different institutions involved. The IMF – with its universal membership and unique financing mechanism – embodies the ultimate safety net on a global level in a uniform way for its member countries. The recent doubling of its permanent quota resources, together with a steady decline in credit outstanding since the crisis peak, puts the Fund in a comfortable financial position and provides confidence that it will be able to fulfil its role as crisis lender for countries in need, also in the unlikely event of a widespread and systemic shock. Here, appropriate communication could help the Fund counteract the perception of a ”stigma“ associated with IMF engagement, by re-emphasizing the notion of a “seal of approval” that goes along with the adoption of an IMF-supported program. At the same time, we like to emphasize the surveillance function of the Fund that constitutes the first line of defense of the global safety net. For the Fund to be successful in strengthening traction of its surveillance and reducing perceptions of the so called “stigma” of using, or even considering, Fund supported programs, it is of the essence that its advice is adequate, consistent and convincing, focusing in particular on macro-critical issues.

With regard to the discussion on a reform of the GFSN, we underscore the need for a well-balanced perspective that appropriately takes into account the crucial contribution for a stable international monetary system building on a strengthened resilience of individual economies. Strong domestic policy action to increase resilience, including the build-up of sufficient own reserves, coupled with strengthened macroeconomic and macro-prudential surveillance, is a key priority for effective crisis prevention. The discussion, therefore, should avoid putting too much emphasis on the further expansion of financing or insurance elements, which may not become available in the short term. When discussing specific proposals on how to further develop the GFSN, we should assess these not only in terms of their ascribed benefits, but also duly take into account potential drawbacks. We need to make sure that reforms are consistent with the mandates of the institutions that make up the GFSN. This sets limits on the possible level of coordination among the different layers. We also need to safeguard the financial integrity of the system and its institutions, first and foremost the IMF. Thirdly, reforms to the GFSN must not give rise to moral hazard or undermine appropriate incentives for strong, stability-oriented policies at the national level. Germany welcomes the Fund’s intention to continue to assist low income countries as well as fragile states.

**IMF Resources**

The successful implementation of the 2010 Quota and Governance Reforms has considerably contributed to strengthening the Fund’s credibility and legitimacy. The Fund is now well bolstered with permanent resources in a size which allows fulfilling its mandate. We particularly welcome the rebalanced composition of Fund resources towards quota resources, which ensures a fair global burden sharing in terms of members’ financial contributions and a better alignment with voting shares. Looking ahead, we see the Fund adequately equipped with its own quota resources, while the supplementary New Arrangements to Borrow serve as a backstop to cover tail risk scenarios.

**Sovereign Debt Restructuring**

Germany welcomes the Fund’s progress with regard to its agenda on sovereign debt restructuring issues. In particular, we strongly support efforts to strengthen the market-based contractual approach to facilitate more timely and orderly sovereign debt restructurings, should the need arise. In this regard, we appreciate the inclusion of enhanced collective action and modified pari passu clauses in new issuances of international sovereign bonds. We encourage the IMF, in consultation with other relevant parties, to further promote and monitor the use of the strengthened bond clauses. Moreover, we look forward to the forthcoming IMF analysis on private sector involvement in the context of its lending into arrears policy for private creditors, which will complete the Fund's sovereign debt restructuring agenda agreed in 2013.

**Special Drawing Rights**

We welcome that the Renminbi has been determined a freely usable currency by the IMF and will be included in the SDR basket in October this year. We encourage the Chinese authorities to continue and deepen their reform efforts which have contributed to advance the Renminbi to an international reserve currency.

As the 10th basis period comes to a close soon, the next quinquennial review of a General Allocation of SDRs will be on the agenda. As in the past, the Executive Board will have to decide for the forthcoming 11th basis period whether there is a „long-term global need to supplement existing reserve assets“, that, according to the Fund's Articles of Agreement, is the prerequisite for a general SDR allocation. We are looking forward to the staff's analysis, which will need to take into account also the strong increases in national reserves in many countries over past years, and the very sizeable SDR allocations in 2009.