International Monetary and Financial Committee

Twenty-Ninth Meeting
April 12, 2014

Statement by Eveline Widmer-Schlumpf,
Head of the Federal Department of Finance,
Switzerland

On behalf of Azerbaijan, Kazakhstan, Kyrgyz Republic, Republic of Poland, Serbia, Switzerland, Tajikistan, Turkmenistan

International Monetary and Financial Committee (IMFC), April 12, 2014

Statement by Ms. Eveline Widmer-Schlumpf, Minister of Finance of Switzerland on behalf of Azerbaijan, Kazakhstan, Kyrgyz Republic, Poland, Serbia, Switzerland, Tajikistan, and Turkmenistan

I welcome the Managing Director's messages to policymakers in her *Global Policy Agenda* (GPA). I also broadly share her views about how the IMF can help its members implement this agenda. In what follows, I want to emphasize the aspects that I view as critical.

I. MONETARY NORMALIZATION AND POLICY SPILLOVERS

Macroeconomic policy stimulus, in particular monetary policy easing, has created essential breathing space. However, it will not lead to strong, sustainable, and balanced growth in and of itself. As such, this policy stimulus has been a necessary yet is not a sufficient condition for the global economy to turn the corner to lasting growth. Further policy action remains indispensable, in particular in the areas of structural reforms, fiscal consolidation, as well as balance sheet repairs for households, financial institutions and corporates. The longer policymakers delay their reform efforts, the more scope there will be for the potential unintended consequences of policy stimulus to materialize.

We would also have appreciated a clearer emphasis on (i) the potential side effects and unintended consequences from the prolonged use of unconventional monetary policies, (ii) the sizeable macroeconomic imbalances in a number of key emerging market economies, and (iii) the large stock of non-performing loans in stressed euro area countries. These risks need to be promptly and decisively addressed with appropriate policy actions.

The recommendation for accommodative monetary policies in advanced countries is too broad. It should be more nuanced. The possible risks posed by too low inflation should be more thoroughly qualified by taking into account the precise structural, economic, financial and monetary conditions of the region or the country in which it occurs. By contrast, we would highly welcome a clearer acknowledgement of potential risks to financial stability arising from prolonged monetary easing.

We are of the view that the recent differentiated deterioration in emerging market economies owes largely to domestic macroeconomic conditions. While domestic vulnerabilities may vary across countries, they point to the common need for strong policy buffers at all times. Indeed, those countries that have adopted prompt and decisive policy responses in the past have fared better in recent months. We continue to think that the ongoing adjustment in some countries might also represent a return to a more sustainable steady state, which is not necessarily an unwanted development. Lastly, we welcome the Fund's focus on multidirectional spillovers across regions of the global economy.

II. Ensuring Robust, Sustainable Growth and Reducing Vulnerabilities

We welcome policy recommendations to raise potential growth and thus to lower the risks of stagnation. The focus on monetary policy accommodation should not detract from much needed structural policies. We would appreciate more emphasis on the sizeable expected gains from labor and product market reforms, as well as infrastructure projects. In many countries, deeper structural reforms, bank and corporate balance sheet repair, and institutional reform are needed to address long-term impediments to competitiveness and productivity. We concur that reform fatigue is a key risk in this respect.

While flexibility in fiscal policy can play a role in supporting growth in the short term, the priority for many countries is to reduce their significant fiscal vulnerabilities. Stronger efforts are necessary to bring down public debt ratios over the medium term. Such safe levels are likely to be lower than pre-crisis levels in many countries. In this context, we welcome the focus on public expenditure reforms and on supportive institutional arrangements. Ultimately, what matters is the entire fiscal framework, in particular its design and legal anchor.

Effective fiscal consolidation requires an appropriate combination of measures. Even though expenditure reforms are often politically difficult, they deliver important long-run benefits in terms of fiscal sustainability. The short-term contractionary impact of fiscal consolidation should not lead to inaction but instead calls for a balanced approach over the medium term. Consolidation efforts targeting government consumption should be prioritized, as cuts in public investment, as well as in physical and human capital, hamper economic growth in the long run. Moreover, the negative effects of fiscal consolidation can be limited by striving for a more efficient provision of public goods and services.

We would welcome further work on fiscal rules and institutions, given their key role in sustaining fiscal consolidation over time. Care should be taken to include the fiscal position as a whole in the design of reforms. For example, expenditure rules are transparent, easy to implement and monitor. However, on their own, they do not ensure debt sustainability as they leave the revenue side completely out of consideration. It would therefore seem warranted to combine expenditure rules with a rule directly aimed at fiscal sustainability, such as a balanced budget rule or a debt rule.

The financial sector regulatory reform agenda is not yet complete, and reform momentum must be maintained. This applies to ending the "too-big-to-fail" problem, the work on risk weighting and accounting convergence, and the current reform efforts for OTC derivatives markets and shadow banking.

While at a national level progress is being made, work should continue to make cross-border resolution of systemically important banks effective. In this respect, cooperation between national authorities should be strengthened. Ensuring an orderly resolution of "too-big-to-fail" institutions without recourse to public funds ("bail-outs") should also remain an important policy objective. We are of the view that it is both possible and socially desirable to devise resolution strategies that do not rely on public funds. We should strive to avoid sending signals that could undermine efforts to develop such resolution plans. In this sense, we fully support the work on the adequacy of gone-concern loss absorbing capacity.

III. Adapting the Fund to the Changing Global Economy

While we welcome that the Fund continuously strives to adapt to the changing world, we emphasize that the Fund has been most successful when it remained focused on a limited number of well defined tasks. We should not forget that the core mandate of the institution is, and should remain, the stability of the international monetary and financial system. In this context, the Fund's contribution to debates such as international taxation, the interplay between fiscal policies and inequality, and issues related to aging or environmental change should remain consistent with its core mandate.

We endorsed the proposal to modify the methodology for determining systemically important financial sectors, which increased the number of countries subject to mandatory FSAPs from 25 to 29, including Switzerland and Poland. The new methodology to identify jurisdictions with systemically important financial sectors is a welcome improvement. Financial interconnectedness has become an increasingly important focus of the Fund's work. In turn, we expect that the central role of interconnectedness will be recognized in other important areas, such as the governance framework.

We welcome the review of the Fund's crisis prevention and resolution tools, including the Flexible Credit Line (FCL). The renewals of the FCL arrangements by three countries, including Poland, should be viewed in the context of the severity and long-lasting consequences of the global financial crisis. At the same time, we acknowledge that reliance on a FCL arrangement has never been meant to be permanent and thus we support work facilitating discussions on exit strategies.

The absence of a robust framework for restructuring sovereign debt represents a gap in the international financial architecture. Debt restructuring – as a solution of last resort – must find acceptance. More orderly procedures, such as adaptations of sovereign debt contracts, need to be complemented by clear limits on official financing. These are needed to ensure that the burden of resolving crises is shared even-handedly among private and official creditors. By reducing creditor and debtor moral hazard, a reliable framework for sovereign insolvency would act as a deterrent. This, in turn, would help improve the assessment of sovereign bond risks ex ante, making debt overhangs and crises less likely in the future. In the meantime, current sovereign debt overhangs have to be addressed based on existing practices and institutions, and – if unavoidable – through extraordinary one-off measures. We urge the Fund to bring forward this comprehensive agenda for making the international financial architecture stronger.

We reiterate the importance of fully implementing the 2010 quota and governance reform. We continue to see the entry into force of the 2010 reform as a prerequisite for meaningful discussions on the Fifteenth General Review of Quotas. These discussions should start with an in-depth assessment of the role and size of the Fund in the longer run. The discussions on a new quota formula will have to be integrated and move in parallel with the discussion on the Fifteenth Review. As a matter of legitimacy, any revision of the current formula should better capture the dimension of interconnectedness of economies via international trade and finance. Substantial voluntary financial contributions to the Fund by members should be accounted for in the distribution of quota shares. We are of the view that the discussion on quota and governance reforms must continue to take place in the Fund and the IMFC to ensure that the process remains inclusive and consistent with the rules-based character of the Fund.