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Statement by Piercarlo Padoan,
Minister of Economy and Finance, Italy

On behalf of Albania, Greece, Italy, Malta, Portugal, San Marino

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Developments in the Constituency

The business cycle of almost all the countries in the constituency improved in second half of 2013. This is in line with the evidence for the euro area. Portugal and Italy returned to a positive rate of GDP growth in the third and fourth quarter of the year, respectively. Malta's expansion remained robust and Albania kept growing, despite some slowing down. In Greece the adverse cyclical phase lessened significantly and expectations project a positive turning point in 2014 after a harsh and long-lasting recession. Also in San Marino the decrease of GDP eased somewhat. For all the countries of the constituency, macroeconomic projections foresee the acceleration of economic activity in 2014, driven by a partial strengthening of domestic demand and the continued support from net export. The consolidation of the recovery might also contribute to an increase of inflation from the currently undesirable low levels in several countries of the constituency.

The current account balances significantly improved in 2013. Across the constituency, the surpluses have been also the result of noticeable efforts to regain competitiveness, thus highlighting structural improvements. Albania is still featuring a deficit and authorities are committed to productivity-enhancing reforms.

Despite the generally enhanced economic outlook, labor market conditions remain diffusely difficult, except for Malta. Unemployment rates are still high, particularly among the young, and call for renewed reforming efforts to enhance job creation.

Fiscal consolidation continued in 2013 and targets were broadly met. In Greece and Portugal, achievements were better than expected by a sizeable margin. In the current year, fiscal adjustment is projected to continue in the constituency, though with a lower drag on economic growth. Italy will be one of the EU countries with the lowest deficit-to-GDP ratio.

Also in the financial sector, the situation keeps improving. Banks managed to increase their capital ratios resorting to private funds amidst a challenging cyclical phase. Sovereign interest rates substantially decreased. In Italy and Portugal they are at historically low levels. Nonetheless credit flows remain anemic, reflecting the persistent financial fragmentation in the euro area. However, the latter is expected to ease also as a result of the entering into force of the European Banking Union.

In the constituency, there are currently three IMF supported programs. In Greece, the Troika just reached a staff-level agreement with the Greek government on the Fifth Review.

Impressive achievements were realized in fiscal consolidation. A large number of structural reforms has been implemented in all sectors of economic activity. Portugal is approaching the end of its economic and financial assistance program. Implementation has been strong and a firm commitment to credible policies will continue to be fundamental. In Albania, the government recently signed an arrangement with the IMF under the Extended Fund Facility (EFF), which will be used to clear the arrears, ensure fiscal consolidation, improve debt sustainability, and support the reform program.

Developments in the Members of the Constituency

Italy: A newly appointed Government is boosting the reform process already under way in order to make the recovery more robust and sustained over the medium term. The most noteworthy measures to tackle the long-standing obstacles to achieving Italy's competitive potential include: 1) a major labor market reform to encourage hiring and bring more people into the labor force, through more entry/exit flexibility combined with the simplification of employment contracts and an extension of the social safety net; 2) an extensive reform of the public administration through a broad-based spending review to make targeted and structural cuts, as well as fundamentally restructure the delivery of public services; 3) revisions to the Constitution and the electoral law to make Italy's legislature more responsive and effective; 4) an acceleration of the privatization process, also to achieve efficiency; 5) a tax reform to sharply reduce taxation on labor, both for employers and employees; 6) a reform to accelerate the civil justice system; 7) the Destination Italy initiative to attract foreign investment and improve the business environment through simplifications; 8) a further liberalization of product markets; as well as 9) enhance schools and universities.

In terms of recent economic developments, the outlook for the Italian economy has improved since the second half of 2013. After a deep recession - Italy lost about 9 percent GDP from the pre-crisis peak in the third quarter of 2007 - activity stabilized in mid-2013 and then recovered slowly in the final part of the year. Recent leading indicators show additional improvement, with reduced drag from fiscal consolidation and gradually stabilizing credit conditions. Recently approved official forecasts predict GDP growth of 0.8 percent in 2014, steadily increasing thereafter to growth rates approaching 2.0 percent by 2018, benefitting from enhanced potential growth as a result of ongoing structural reform efforts.

The external position of the economy has improved since 2011. In 2013, the current account shows a 0.8 percent of GDP surplus. Following a 2.7 percentage point contribution in 2012, net exports lifted GDP growth by 0.8 percentage points in 2013. While investment activity stabilized in the second half of 2013, consumption remained rather weak. Some leveling off in real disposable income and rising consumer confidence should support private consumption through 2014.

The labor market conditions remain difficult, with the unemployment rate reaching very high levels, especially among the youth. It is therefore of paramount importance to ensure that the recovery will be robust enough to absorb unemployment.

The conditions of loans supply have become less tight in the past months, especially for households. This is supported by the narrowing of government bond spreads, and improvements in the banks' funding, recapitalization of banks and some stabilization in non-performing loans. The negative annual decrease in lending to the private sector has been partly offset by a number of initiatives launched by the Government, including the payment of arrears by the public administration; large firms are in a better situation as they have been able to tap the market by issuing bonds.

Net borrowing declined to 3.0 percent of GDP in 2012, and stayed at the same level in 2013. The primary surplus in 2013 was one of the highest in the EU, amounting to 2.2 percent of GDP or 4.5 percent of GDP in structural terms. Poor nominal GDP dynamics, one-off measures to ease credit conditions, and financial support to other Euro Area Member States resulted in a relatively slight increase in the debt-to-GDP ratio to 132.6 percent in 2013. According to Government projections, the debt-to-GDP ratio will peak in 2014 before declining thereafter. Fiscal consolidation will continue, although at a more gradual pace, with an almost-balanced budget in structural terms already expected in 2015. The ongoing and future privatization process will generate expected proceeds of about 0.7 of GDP per annum.

Albania: Economic growth slowed down during 2013, reflecting both the cyclically weak aggregate demand and the increased uncertainty surrounding the mid-year general elections. Aggregate demand remains constrained by low business and consumer confidence, subdued domestic demand, difficult external environment and tight financing conditions. Economic growth declined to an expected annual rate of 0.5 percent in 2013, while inflation averaged 1.9 percent throughout the year. The lower growth figures have had their effect on credit, whose dynamics turned negative during 2013.

With due regard to macroeconomic stability, the Albanian authorities have progressively engaged in countercyclical policies. The monetary stance has been made more expansionary, given the clear rationale provided by the weak underlying inflationary pressures and the negative output gap. The Bank of Albania lowered the interest rate by 1 percentage point to historical lows during the year. Moreover, the Central Bank implemented a series of macroprudential measures to tackle the negative credit growth and improve credit quality. A series of laws were also passed, to unburden the bank balance sheets and improve the financial stability indicators. All in all, the financial system remains well-capitalized and able to withstand pressures from domestic and foreign markets, as was evaluated on the latest FSAP conducted by the IMF in December. Coupled with the expansionary monetary policy, this package of measures has started having effect on the economy, by slowing down the growth of non-performing loans and lowering financing costs throughout the economy.

With rising public debt and limited fiscal space, fiscal policy has been cautious and fiscal stimulus low. At the end of last year public debt reached over 70 percent of GDP and is projected to rise further during 2014. The government signed a new arrangement with the IMF under the EFF program, which will be used to clear the arrears, ensure fiscal consolidation and improve debt sustainability, and support the reform program. Fiscal consolidation will take into account the cyclical position of the economy, so that it does not hinder GDP growth. The parliament agreed on new tax measures, mostly addressing the revenue side. The country moved away from flat personal income and profit taxes, to a higher rate progressive system.

The overall policy mix has been largely successful in preserving macroeconomic stability. The on-going fiscal adjustment and the broadly stable economic and financial environment will provide a solid basis for balanced growth for the country. Notwithstanding, the Albanian economy is in need of structural reforms to increase productivity, address labor market rigidities and improve competitiveness. The authorities remain committed to tackle this issue through an ambitious and detailed reform agenda.

Greece: The economic situation in Greece has improved dramatically during the last few months. After six years of persistent negative growth rates, the Greek economy is expected to expand by 0.6 percent in 2014, based on a better-than-expected outcome in 2013, when GDP declined by 3.9 percent, compared with an initial forecast of -4.2 percent. The unemployment rate declined marginally in the third and fourth quarter of 2013 after twenty consecutive quarterly increases. In the external sector, Greece achieved a surplus in the current account balance for the first time in over fifty years. The real effective exchange rate (based on unit labor costs) has been constantly declining since 2009 and Greece managed to regain the competitiveness lost during 2000-2009.

The most impressive achievements were realized in fiscal consolidation. In 2013, both the General Government deficit and the General Government primary balance exceeded program targets. This outcome allows the government to be ahead of schedule in reducing public debt, repaying arrears to the private sector, and supporting the most vulnerable citizens that were heavily affected by the crisis through the distribution of a one-off “social dividend”. Preliminary estimates for the first two months of 2014 indicate that fiscal outcomes continue to surpass program targets.

The situation in the financial sector is also improving. The banking sector is recovering. The latest financial results indicate improved margins and cost containment, as well as a slowdown in the flow of new non-performing loans. Recent stress tests conducted by the Bank of Greece estimated the capital needs of the four systemic banks at €6.4 billion. Two of the core banks have completed larger-than-required capital increases, with significant over-subscription; the total amount raised was €3 billion. The remaining two also expect to draw private capital or otherwise meet their capital needs through own sources by the June 2014 deadline. The liquidity of the banking sector is also improving: deposits have increased since mid-2012, banks have managed to access the money market again, and central bank funding has more than halved.

The Greek Government has implemented a large number of significant structural reforms in all sectors of economic activity, mainly in the labor and product markets, the health sector, the business environment and competition, the public administration and tax governance, and also in liberalizing restricted professions and the energy sector. These reforms have started to bear fruits, as evidenced by the turnaround in economic activity, and the results will be fully visible in the medium-term. Currently the Greek Government is focusing on deepening product market liberalization by implementing a vast array of OECD recommendations.

As a result of these initiatives, investors' confidence in the prospects of the Greek economy has improved and ten-year bond yields have substantially declined. On April 9, 2014 the Greek Government successfully launched a 5-year bond issue at 4.95 per cent yield, which was oversubscribed sevenfold.

Last month the Troika reached a staff-level agreement with the Greek Government on the fifth review of the Fund-supported program and the corresponding review of the EC and the ECB. On April 1, 2014, the Eurogroup considered that the necessary elements are now in place to launch national procedures for the approval of the next EFSF installment of €8.3 billion in 3 tranches, following the full implementation of the prior actions. The IMF Executive Board is also expected to consider the review in the coming weeks.

Malta: The Maltese economy expanded at a relatively fast pace during 2013. Real GDP grew by 2.4 percent in 2013 compared with 0.6 in 2012. Growth was driven by domestic demand, as net exports, though positive, declined when compared to the previous year.

Inflation, measured on the basis of the Harmonized Index of Consumer Prices, decelerated to 1.0 percent in 2013 from 3.2 in 2012, with the year-on-year inflation rate following a downward path during most of the year. The moderation in inflation mainly reflected developments in the prices of services and to a lesser extent those of food, energy and non-energy industrial goods.

During 2013 the labor market remained buoyant with employment continuing to grow particularly in the services sector. Nevertheless, as the labor supply increased significantly, the unemployment rate edged up slightly to 6.5 percent from 6.4 in 2012.

With regard to the balance of payments, the current account registered a surplus for the second year running (equivalent to 1.4 percent of GDP in 2013) underpinned by positive developments in the services balance. The latter offset a deficit on the goods account which continued to widen over the year as a decline in related exports exceeded a fall in imports.

In 2014 the Maltese economy is expected to register a similar level of growth as that achieved in 2013. GDP growth is expected to be underpinned by private consumption and investment. The rate of inflation is projected to pick up moderately driven by services prices, although prices of food and non-energy industrial goods are also expected to contribute. The rate of unemployment is projected to remain unchanged over the year.

The general government deficit to GDP ratio rose above the 3 percent threshold in 2012, but it is estimated to have fallen below that level in 2013, as current revenue is expected to have grown at a stronger pace than current expenditure. Meanwhile, General Government debt is estimated to have reached 71.3 percent of GDP in 2013, up from 70.8 in 2012.

Malta's financial sector remained sound and resilient during 2013. The core domestic banks registered a strong profit performance which contributed to a further strengthening of their capital ratios. Liquidity in the banking market also remained ample. With the setting up of a Joint Financial Stability Board (JSFB) between the Central Bank of Malta and the Malta Financial Services Authority matters related to financial stability were discussed regularly and where necessary addressed. In this regard the JFSB implemented measures aimed at tightening the rules on banks' provisioning practices.

Portugal: Portugal approaches the end of the Economic and Financial Assistance Program. Implementation has been strong, amidst a strengthening economic recovery and improved market sentiment and financing conditions. While the more benign environment facilitates the ongoing adjustment, the still significant challenges facing the Portuguese economy leave no room for complacency.

An annual GDP growth rate of 1.2 percent is now projected for 2014, following -1.4 percent in 2013. The recovery is supported by an improving domestic demand and a continued strong growth in exports. The unemployment rate, although still at a high level, has been gradually declining since the first quarter of 2013 and employment is also recovering. The external adjustment process has continued and in 2013 Portugal registered a net lending position of 2.0 percent of GDP, and a surplus of the trade balance. Inflation is projected to remain at low levels.

The 2013 fiscal deficit objective under the Program was met by a sizeable margin, having stood at 4.9 percent of GDP (4.5 percent excluding the recapitalization of BANIF). This outcome reflects better-than-expected revenue performance and prudent expenditure control, on the back of a continued strong consolidation effort.

Banco de Portugal continues to closely monitor the resilience of the Portuguese banking system. At the end of 2013, liquidity and solvency stood at comfortable levels, although profitability remains under pressure. In the context of the deleveraging process and the rebalancing of the economy, a review of the strategy to facilitate corporate debt restructuring is also ongoing.

Implementation of the ambitious structural reform agenda continued, with significant reforms of labor and product markets and progress on initiatives to promote and facilitate access to finance.

Looking forward, a strong and broad-based commitment to credible and consistent policies remains of the essence to put public and private debt on a clear downward path, to ensure sustainable growth and employment creation in the medium-to-long run and to regain and safeguard full market access. Hence, the adjustment needs to extend beyond the Program's duration, in line with its main pillars, on the basis of a credible and broadly anchored strategy.

San Marino. The consequences of the recent global economic and financial crisis continue to impact on San Marino economic performance, which is still negative. GDP is estimated to have decreased in 2013 and is projected to diminish further in 2014, albeit to a much lower extent. In February, the unemployment rate stood at 9.3 percent.

As for public finance, in 2013 the state budget deficit should amount to about €31 million. In 2014 the deficit is expected to decrease to about €15 million. This objective will be achieved by implementing measures to reduce public expenditure and structural reforms approved to facilitate development and increase revenues. The law on measures supporting economic development and the reform of direct taxation, entered into force on 1 January 2014, are important instruments to attract foreign investments, consolidate Government revenue and stimulate the economic and employment recovery. San Marino has also set up a technical panel for the reform of the indirect taxation system which will result in an alignment with the mechanisms of European tax systems.

Beyond the progress acknowledged by the OECD in terms of compliance with international standards, particularly important was for the Republic the entry into force, on 1 January 2014, of the Double Taxation Agreement with the Italian Republic and San Marino's removal from the Italian black list on 12 February 2014. The alignment process requires time and resources. However, the progress achieved has contributed to bringing some economic stability in specific sectors, such as the banking and financial ones, with a positive outlook for the future. The Central Bank of San Marino has also concluded a first memorandum of understanding with its counterpart in Liechtenstein and it is now in contact with the Central Banks of other States, including the Bank of Italy, to sign other memoranda. Internationalization and increased integration with foreign markets are fundamental steps for future economic growth.

In 2013 the liquidity of banks gradually improved and further consolidation has been achieved through mergers, also aimed at overcoming crises, by transferring assets and liabilities to larger banks. An important result was achieved with San Marino's migration to the Single Euro Payments Area (the so-called SEPA) in February 2014. This is a significant recognition of the progress made by the country also in view of greater integration of the banking sector with the European capital market.

The structural reforms already approved and aimed to enhance competitiveness and doing business are producing early signs of potential trend reversals, stimulating renewed interest from foreign investors. The evolution of San Marino's economic system will also be favored by the official negotiations on the association agreement with the EU, which are due to start in the coming months.

Looking ahead, San Marino's economy will face significant challenges. However, the reforms already adopted and the ongoing efforts have started to bear fruits and contributed to the establishment of milestones for a new phase of economic growth.

Role of the IMF

Surveillance

Earlier this year the Fund has revised its strategy on Anti-Money Laundering and Counter Financing of Terrorism (AML/CFT) issues, endorsing the revised Financial Action Task Force (FATF) Recommendations and the New Assessment Methodology, now including a risk-based approach. These issues are very relevant since possible shortcomings in the implementation of an adequate AML/CFT framework might have a significant detrimental impact on macro-economic and financial stability. In this vein, it is essential to continue to convert all FATF assessments into the IMF Reports on Observance of Standards and Codes (ROSC) and to provide timely and accurate AML/CFT input into the Fund Financial Sector Assessment Program (FSAP). It is also crucial to further enhance the well-established cooperation among international institutions with a view to continuously increase the surveillance quality standards.

Low-Income Countries (LICs)

Over the years, Fund's role in supporting Low Income Countries has been increasingly important. Sustaining LICs' long-term macroeconomic stabilization now requires calibrated interventions, making them more anchored to regional characteristics, specific conditions, and correct incentive mechanisms.

The ongoing revision of the Fund's Debt Limit Policy is a key process to achieve these goals. In particular the Fund should seek the way to guarantee LICs greater access to different financing sources; this requires higher flexibility, and we believe that the proposal for a new single debt limit, including both concessional and non-concessional borrowing, goes in this direction. At the same time the incentive for LICs in seeking concessional funds should be kept strong, so to ensure that the resources financing the Poverty Reduction and Growth Trust (PRGT) are used effectively. On this point, we strongly support the criteria of self-sustainability of the PRGT, and encourage to expand, when possible, the fund raising process to new potential third parties.

Finally, it is extremely significant to reaffirm Fund's importance in supporting growth in LICs. On this point, the Fund has correctly recognized the key role of upgrading traditional crucial sectors, like agriculture, and the role of economic diversification, as it is conductive to faster growth, lower output volatility and ultimately to economic development. Structural reforms are generally essential to underpin diversification and growth, and the Fund should continue to seek the most appropriate tools to encourage and support the process of reforms.

Governance

The implementation of the 14th General Review of Quotas remains crucial to preserve the Fund's credibility and effectiveness. Looking ahead, we are committed to the timely completion of the 15th General Review of Quotas, including an agreement on a quota formula. In this regard, it is of the essence to envisage a balanced and comprehensive package - that deals contemporaneously with all the elements that contribute to the quota formula - and with a spirit of compromise by the whole membership.

IMF Facilities

The Fund's lending facilities include precautionary instruments, which play an important role as they strengthen the crisis prevention toolkit, create incentives for good economic management, and prevent excessive reserve accumulation. The recent review of precautionary facilities pointed to the need to maintain such facilities in the Fund's toolkit. Going forward, it will be essential to increase transparency on the qualification criteria and the level of access. In this regard, further work will be done to develop an indicator of external stress since a clear assessment of external risks is a decisive element to decide about access and exit from such facilities. Additionally, selected indicators of institutional strength will also be elaborated.