International Monetary and Financial Committee

Thirty-First Meeting
April 18, 2015

IMFC Statement by Joaquim Levy
Minister of Finance, Brazil

On behalf of Brazil, Cabo Verde, Dominican Republic, Ecuador, Guyana, Haiti, Nicaragua, Panama, Suriname, Timor-Leste, Trinidad and Tobago

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World economy

1. Since the last IMFC meeting in October 2014, the world economy was unable to show strong signals that it has fully recovered from the 2008 financial and fiscal crises, bringing the prospect that a "new mediocre" would prevail in our discussions. Fortunately, many of the risks related to the recovery of economic activity in the Euro area and the United States, to the debt sustainability of some major European countries, or even to the possibility of a sharp slowdown in China have not materialized.

2. At this time, countries in the Euro area are experiencing a successful fiscal adjustment, but problems related to stagnation and unemployment remain, particularly among the younger population.

3. China is pursuing its strategy to shift the growth driving force towards consumption. The growth model based on investment and exports, with the two variables expanding well above GDP, showed signs of exhaustion in reaction to greater urbanization and the rise in unit labor costs. The fall in investment return rates and the uncertainties related to shadow banks and the housing market have also been sources of investors' concern. But a successful shifting of growth drivers is possible and will do well for China and for the world.

4. Japan is seeking to increase consumers and business confidence. The economic policy known as 'Abenomics' has been conducted through the combination of expansionary fiscal policies coupled with rapid monetary expansion and an aggressive program of securities repurchase. The rise of inflationary expectations has brought down real interest rates and promoted a significant depreciation of the yen. However, exports did not respond to these stimuli as expected and the current account deficit continues to be adversely affected by headwinds of the 2011 tsunami.

5. In Europe, an important part of the economic scenario improvement is due to higher growth rates in the United Kingdom, Germany and Spain, with 2015 GDP growth projected at 2.7%, 1.6% and 2.5%, respectively. Improvements in financial conditions and a new round of euro depreciation are expected with the beginning of large-scale quantitative easing by the European Central Bank (ECB).

6. With regard to Greece, we hope that a debt agreement be reached soon, as we believe it is the best solution to Europe. Unlike previous periods in which Euro area countries were financed with similar interest rates, in the future countries with different fundamentals will probably incur distinct long-term interest rates.

7. In this transition period towards greater economic stability, monetary authorities should pay closer attention to the recent movements in oil prices and to the high volatility of exchange and interest rates. It is not clear how the global economy will adjust to these changes and who will be the winners and losers in this new scenario.

8. In the United States, the economic recovery continues, led by the expansion of investment, industrial production and the gradual increase of consumption, allowing for economic growth above potential. In the labor market, the economic expansion maintains a positive trend in terms of net jobs creation, bringing unemployment to close to its natural rate. Labor cost increases remain below productivity growth, indicating that the expansion of economic activity may continue without significant inflationary pressures. However, some warning signals are beginning to emerge regarding inflation (excluding the energy component), which is getting closer to the long-term target set by the Federal Reserve. This scenario reinforces the view of a possible reversal of the monetary policy followed in recent years.

9. The increase in the Federal Reserve policy rate will probably result in a new round of appreciation of the dollar. In terms of real exchange rate, over the past twelve months, the dollar has appreciated more than 20% against the euro, 12.7% in comparison with the British pound and 17.5% against the Japanese yen. If the current level of the real exchange rate is maintained, or if the dollar appreciates further, the fall in net exports may eliminate an important part of US growth in coming years.

10. The divergences between monetary policy in the US, on the one side, and the Euro area and Japan, on the other, can have significant impact for emerging market and developing countries (EMDCs).

11. The normalization of monetary policy in the US will possibly lead to an increase in speculative short-term capital movements with potential adverse effects on financially open EMDCs. However, the dollar appreciation may lead to a rebalancing of US growth towards higher consumption with lower inflationary pressures. This means that the interest rate path may follow a more moderate increase than it would be observed in the absence of exchange rate movements.

12. EMDCs with dollarized economies or currencies pegged to the US dollar are among the countries most affected by its appreciation. We have a number of such cases in our constituency. A period of prolonged US dollar strength could undermine their competitiveness and external positions.

13. Since the last IMFC meeting, Brazil has adopted a new set of policies to restore fiscal balance and prepare the economy for a new investment and growth cycle. These policies consider both the uncertain scenario for the global recovery, as discussed above, as well as the need to readjust fiscal policies and roll back countercyclical measures to cope with the end of the commodity cycle.

14. The current year is a transition year for the Brazilian economy, when we are committed to a swift reversal of the fiscal situation towards stable and eventually declining debt ratios. Fiscal balance is a necessary condition for growth resumption, but more needs to be done. Hence, economic and monetary authorities in Brazil are also working with Congress on a broad agenda of structural changes to improve the business climate, increase productivity and set price signals correctly to stimulate investment. Structural changes include not only reform of the pension system and unemployment benefits and a reassessment of tax exemptions, but also a host of measures to instill new dynamics to the capital markets and foster long-term infrastructure investment. Together, the fiscal and the structural growth agenda aim at protecting the social gains of the last decade and strengthen the new middle class, offering social inclusion through new opportunities.

15. Given the diversity of our labor force, the vigor of the Brazilian private sector and the soundness of Brazil's financial system, we expect a relatively quick reallocation of resources and the recovery of growth, driven by growing exports, among other factors.

IMF reforms

16. The Fund's quota-based nature and its legitimacy and effectiveness remain at risk. By continuing to delay the ratification of the 2010 reforms, the US thwarts the increase of the IMF's quota resources and the realignment of quotas and voting power, as agreed almost five years ago.

17. This delay not only disappoints the countries in our constituency and the membership at large, but also jeopardizes the Fund's lending capacity, which remains heavily dependent on borrowing, especially from the New Arrangements to Borrow (NAB). As we all know, the Fund relies deeply on the continuous support of the NAB, a voluntary mechanism subject to half-year renewals. We have to guarantee a permanent and reliable capital base to the Fund and restore its quota-based nature.

18. The IMFC has reaffirmed the importance of the IMF as a quota-based institution and that the implementation of the 2010 reforms remained the highest priority. The IMFC also decided in April last year that if the reforms were not ratified by end-2014, the IMF should stand ready with options for next steps. This guidance was endorsed by G20 Leaders in their Brisbane Summit last November. Since January, the Fund's Executive Board has been meeting to discuss interim options, pending the full implementation of the 14th General Review of Quotas (GRQ).

19. Among the interim options, we have indicated our preference for delinking the quota reform from the Board reform amendment. The delinking proposal provides political assurances

that it would not modify decision-making in the Fund. In the case of the ad hoc option, we do not have any assurances that it will deliver a result sufficiently close to the 2010 reforms to make it worthwhile, nor that it will be truly temporary.

20. We are also disappointed that work on the 15th GRQ has not yet even started. We urge the Fund to take up this work with no further delays, including delivering on the commitment to agree on a new quota formula.

BRICS New Development Bank and Contingent Reserve Arrangement

21. In November 2014, BRICS Leaders met on the margins of the G20 Summit in Brisbane and expressed their commitment towards the expeditious implementation and ratification of the agreements signed in Fortaleza, Brazil in July 2014 on the New Development Bank (NDB) and the Contingent Reserve Arrangement (CRA).

22. The NDB will be headquartered in Shanghai and is expected to start operations in 2016. An Interim Board of Directors, designated by the five BRICS countries, is working on the preparation of the NDB. The management team will be designated well in advance of the next BRICS Summit in Russia, in July. In Brisbane, it was also agreed that the New Development Bank Africa Regional Center will be established in South Africa concurrently with the headquarters.

23. The purpose of the NDB will be to mobilize resources for infrastructure and sustainable development projects in BRICS and other emerging and developing economies, supplementing the efforts of multilateral and regional financial institutions. Membership of the NDB will be open to all countries.

24. Work on the CRA is also progressing, according to the timetable established by the BRICS Leaders in Brisbane. The entire operational structure, including the Inter-Central Bank Agreement foreseen in the CRA Treaty, is expected to be concluded by the next BRICS Summit.

Small developing states

25. The IMF continued to advance its agenda for small states. In March 2015, the Executive Board discussed a staff report on small developing states", which highlighted key issues pertaining to their recent macroeconomic developments. Small states have limited resources to produce their own macroeconomic research and thus tend to rely more heavily on the Fund. As a constituency that includes five small states – CaboVerde, Guyana, Suriname, Timor-Leste, and Trinidad & Tobago – we welcome this discussion and encourage the Fund staff to make good use of it to leverage the Fund's engagement with this segment of the membership, particularly in surveillance, lending and technical assistance.

26. There is considerable additional work to be undertaken by the IMF on small states issues, and we urge the Fund to keep this work as a top priority. In this regard, we suggest that small

states be included among the target groups in any review of the Fund's lending instruments. We also invite the Fund to integrate more fully the limited production and export bases and high vulnerability to natural disasters in future analyses. Finally, the discrepancy between income classification and economic resilience of certain small states is also an important topic to be addressed as part of the discussion of funding for development and fiscal sustainability.

Countries in fragile situations

27. Two countries in our constituency – Haiti and Timor-Leste – have taken a leading role in advocating the agenda of fragile states, notably in the context of the g7+, an association of 20 countries that are or have been affected by conflict and are transitioning to a next stage of development.

28. The Fund plans to assess the adequacy of its lending instruments for countries in fragile situations, as stated in the Managing Director's April 2015 Global Policy Agenda. The heterogeneity of the countries that fall in that group calls for tailored approaches. We are particularly concerned with the challenges faced by those that are at the same time fragile and small, as they also have to overcome the constraints inherent to their size. We hope that the IMF will take a leading role in encouraging development partners to strengthen their engagement with member countries in fragile situations.

29. We welcome the creation of the Catastrophe Containment and Relief (CCR) Trust, building on the previous Post-Catastrophe Debt Relief (PCDR) Trust, which allows the Fund to respond to a wider spectrum of humanitarian crises. Through the CCR and other instruments, the Fund has been able to react timely to the Ebola crisis, delivering much needed support to the three countries most affected by the disease, all of which g7+ members.

30. We are also pleased that, under the initiative of our constituency, a Working Group of IMF Executive Directors representing countries in fragile and conflict-affected situations was formed to coordinate their actions in the Executive Board and strengthen the quality of the cooperation between the Fund and these countries.