International Monetary and Financial Committee

Twenty-Eighth Meeting
October 12, 2013

Statement by Fabrizio Saccomanni,
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On behalf of Albania, Greece, Italy, Malta, Portugal, San Marino

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Washington, October 11-12, 2013

Developments in the Constituency

In the second quarter of 2013 the euro area economic growth turned slightly positive, interrupting a recession that had started at the end of 2011. According to the most recent conjunctural indicators, the recovery should continue in the second half of the year, although at a moderate pace.

In this context, the economies of the Constituency also showed signs of improvement, or at least of a less unfavorable outlook. In some of them (Portugal, Malta and Albania) GDP increased by a rather sizeable amount in the second quarter; in others (Italy) the adverse cyclical phase lessened somehow, and expectations point to a positive turning point toward the end of this year. In Greece, where the recession is still harsh, some early signs of the fruits borne by the impressive efforts undertaken so far are emerging and a moderate GDP growth is forecast for 2014. In San Marino, the intense reform process is expected to deliver positive results soon.

Indeed, some of the drivers behind these developments are country-specific (see following paragraphs). In general, however, external demand is still providing the major support to economic activity, with positive effects on the rebalancing of current accounts. On the other hand, domestic demand continues to languish, particularly in countries undertaking consolidations of public finances; the fiscal drag on growth should gradually lessen over the next few years. Also the euro area financial fragmentation is taking a heavy toll: monetary transmission mechanisms are still partly impaired, resulting in relatively high interest rates and contributing to weak credit flows. Efforts to strengthen the resilience of the banking sectors are continuing, despite headwinds coming from the effects of a prolonged economic crisis.

Greece and Portugal are still under IMF-supported programs. Greece has completed the Fourth Review and is currently negotiating the completion of the Fifth Review. Major progress has been achieved in fiscal consolidation and in labor market reforms. Structural reforms had fallen behind schedule until June, but a new coalition government that was formed at that time has re-energized many important areas, such as public sector restructuring and product and services liberalization. In Portugal, program implementation is progressing at a good pace. On the joint 8th and 9th review mission, early signs of recovery led to an upwards revision of economic prospects. As the program reaches its final phase, there is the recognition that maintaining the adjustment efforts and sound policies are crucial for a successful return to market financing.

Developments in the Members of the Constituency

Italy: The outlook for the Italian economy is improving, following eight consecutive quarters of GDP contraction, in line with the pace of European recovery and as a result of the anti-cyclical measures undertaken by the new Government that took office in May 2013. In July 2013 the EU terminated the excessive deficit procedure. The support to recovery was implemented while keeping public sector nominal deficit within the limits agreed at EU level.

GDP is projected to recover to 1.0 and 1.7 percent in 2014 and 2015 respectively, helped by stimulus measures stemming from the acceleration of payments of government arrears (3.2 percent of GDP over a four-quarter period; about 0.7 percent already paid by mid-September) and sizeable incentives to investment in various sectors such as infrastructure development and construction. Structural reforms, initiated by the previous Government and under implementation by the current Administration, are also expected to provide support to the growth outlook.

Leading indicators show moderate recovery in economic activity. Industrial production is also expected to strengthen over the coming quarters. In addition, net export contribution continues to be positive and sizeable, with a substantial improvement in the external position of the country. The current account balance turned into positive territory at 1.4 percent of GDP in the second quarter of 2013.

On the fiscal side, on October 9th, the Government took additional measures to ensure that the public deficit would remain within the 3.0 per cent threshold for the remainder of the year. In structural terms, the budget is already close to balance, which will be achieved in 2015 and kept afterwards.

The debt-to-GDP ratio, inclusive of the financial support to other Member States of the euro area and payments of government arrears, following the peak expected this year, will decline to 120.1 per cent in 2017. This will result from sizeable and rising primary surplus, which is already among the highest in the euro area. Privatization proceeds will also contribute by 0.5 percent of GDP per year, partly due to the setting up of a special vehicle, which is already operational, for collection and subsequent sale of real estate properties and stakes in companies both at State and local government level.

Albania: Following a 1.6 percent increase in 2012, real GDP is expected to grow at close to 2 percent in 2013 and to improve slightly in 2014. Weak private demand, reflecting balance sheet adjustments and high risk aversion in the real and financial sectors, continues to hamper the economy. Export growth has remained strong, on account of structural improvements in the economy and a more favorable real exchange rate.

Notwithstanding the GDP acceleration of recent years, economic growth is still below potential. From a medium-term perspective, structural reforms are needed to increase productivity and competitiveness, support the tradable goods sector, and reduce rigidities and skill mismatch in labor markets, thus ensuring a sustainable growth path.

Unemployment has remained stable at 12.8 percent and increases in real wages and unit labor costs are subdued. CPI inflation averaged 2.1 percent for the first eight months of the year and current projections do not indicate rising inflation over the medium term.

The current account deficit has decreased during the past three years, but remains relatively large at 10.3 percent of GDP in Q2 2013. The overall balance of payments has been in surplus in 2013, due to high FDI inflows. Despite these improvements, the external position of Albania remains vulnerable due to low competitiveness and savings-investments imbalances in the economy. The resolution of these vulnerabilities is the medium term priority of the Albanian authorities.

Public debt has increased to around 64 percent of GDP, on account of discretionary fiscal stimulus in the run-up to elections but also unexpected fiscal slippages in the form of lower revenues and accumulation of arrears. The Authorities remain committed to take strong and urgent action in order to reverse the trend of fiscal deterioration and to put public finances into a sustainable medium- to long-term path. At the same time, the speed of consolidation will also take into account the cyclical conditions in the economy. It will be geared towards growth-friendly measures, which combine improving the quality and efficiency of public services with minimizing distortionary effects of taxation.

Weak growth has increased difficulties in the real sector, and in turn has been reflected in higher non-performing loans (NPLs) in the banking system, which however remains profitable, liquid and adequately capitalized. Increasing domestic NPLs, tough guidelines imposed by parent groups and tight regulations at Eurozone level, have led to an overcautious approach to lending. Low demand for new loans and supply side constraints are reflected in the negative growth of credit stock portfolio.

In the presence of weak inflationary pressures, monetary policy has turned increasingly expansionary and the policy rate stands at a historical low of 3.5 percent. However, because of the high risk premia, the transmission mechanism of monetary policy has been weak.

Greece: In the last four years Greece has been implementing the most ambitious program of fiscal consolidation and structural reforms among advanced economies. Despite the long recession – 2013 will be the sixth successive year of output contraction that cumulatively amounts to a drop in real GDP close to 27 percent – the achievements so far have been impressive.

By the end of 2013 Greece is expected to achieve a primary surplus, which is a necessary condition for Eurogroup to fulfill its commitment of 27th November 2012 “to provide adequate support to Greece during the life of the Programme and beyond until it has regained market access”. Between 2009 and 2012, the primary deficit (excluding support to the financial sector) declined by 9.3 percentage points of GDP – the biggest and fastest ever recorded adjustment by an OECD economy. The European Commission estimates that between 2009 and 2012 Greece reduced its structural budget balance by 13.8 percentage points of GDP and that in 2013 Greece will achieve a structural primary surplus of 6.3 percent, the highest in the EU.

In addition, the external balance and the competitiveness of the Greek economy have also improved significantly. The improvement in competitiveness is reflected in the rapid fall in the current account deficit from -14.9 percent of GDP in 2008 to -3.4 percent of GDP in 2012, while the IMF projects that the deficit will be nearly eliminated in 2014. Compensation per employee in the total economy fell by 6 percent in 2012 and is forecasted to decline further by 7.9 percent in 2013. Currently, Greece has the lowest inflation rate in the euro area with prices actually falling, for the first time in 40 years, by 1.0 percent in the year to August 2013, compared to a euro area average increase of 1.3 percent. As a result, approximately three quarters of the cumulative loss in Greek competitiveness between 2001 and 2009 vis-à-vis the euro area was recovered by 2012.

In the financial sector, all four core banks have been recapitalized by the Hellenic Financial Stability Fund. Three of the core banks managed to attract at least 10 percent of the required additional capital from private sources and remain under private control. All bridge banks were absorbed by the core banks. Major consolidation has been achieved. There are now only four large banks and a few smaller ones, compared with a situation of 17 banks before the crisis. A new stress test exercise is now being conducted and will be concluded by December. Banks will submit to the authorities appropriately revised restructuring and funding plans, while a major reduction in costs is already underway. All these developments have led to increased confidence and a rise in deposits. In August 2013 private deposits stood 6 percent higher than in August 2012.

Since 2010 Greece has also implemented a large number of structural reforms, covering various sectors of economic activity. Most of them had an immediate fiscal impact (for example, reforms of pensions, public health care, public administration and fiscal governance, etc), while others focused on labor and product markets and enhanced the competitiveness of the economy (for example, liberalization of regulated professions, liberalization of fuel and energy markets, judicial reforms, licensing procedures, fast track process for investments, etc). Finally, the privatization process was revived and a number of state-owned enterprises were transferred to the private sector (such as the State Gaming monopoly and the Gas Transmission Operator).

While the above achievements have come at an extremely high socio-economic cost, recent developments are promising. In 2013, GDP is expected to decline by approximately 4 percent, but moderate growth is forecast for 2014. Unemployment remains extremely high

(27.1 percent), while the rate of youth unemployment in Greece is the highest in the EU – close to 60 percent. However, in the second quarter of 2013, the unemployment rate started to decline marginally.

Malta: In the first two quarters of 2013, the Maltese economy accelerated. The average real GDP growth was 1.7 percent year-on-year (up from 0.8 percent in 2012 as a whole). The major contribution to economic activity continued to come from net exports, as domestic demand fell further. The acceleration of economic activity expected for 2013 should gain further momentum next year.

The labor market remained resilient as employment kept expanding, generally supported by a buoyant tourism industry and a growing services sector. The unemployment rate averaged 6.4 percent during the first half of 2013, unchanged compared to 2012.

In 2012, the external balance turned positive, with the current account recording a surplus of 1.6 percent of GDP. During the first half of 2013, the current account registered a deficit of 0.8 percent. Nevertheless, this deficit was smaller compared with the same period last year, partly as a result of favorable developments on trade in goods and services.

HICP inflation declined during the first eight months of 2013, reflecting movements in prices of services, energy and non-energy industrial goods, with the annual rate falling to 0.7 percent in August (it was 3.2 percent in 2012). Inflation is expected to be slightly higher in 2014.

As regards fiscal developments, the general government deficit widened to 3.3 percent of GDP in 2012, while the debt to GDP ratio reached 72.1 percent. Consequently, in June 2013 Malta was placed once again in the European Union's Excessive Deficit Procedure (EDP). The Government is committed to reduce the deficit ratio to below 3 percent by the end of the year, ahead of the EDP deadline, and to strengthen the fiscal framework.

The domestic financial sector remained robust throughout 2012, though it faced challenges from an uncertain external environment. Banks maintained strong capital adequacy ratios and robust liquidity levels, with the core domestic banks continuing to fund themselves through traditional sources. However, the authorities keep stressing the importance of continued assessment of customers' credit worthiness as well as of augmenting provisions and strengthening capital buffers.

Portugal: There has been significant progress in the adjustment of the macroeconomic imbalances of the Portuguese economy and program implementation has been strong, despite difficult economic conditions, an unfavorable external environment and increased uncertainty and volatility.

After ten consecutive quarters of decline, in the second quarter of the year GDP grew by 1.1 percent over the previous one. Although caution is warranted when analyzing this result, positive signs can also be drawn from the most recent confidence indicators across sectors, pointing to a sustained upturn of the economy. In the same quarter the unemployment rate, although still at a high level, went down to 16.4 percent, from 17.7 in the previous quarter.

The 2012 deficit objective under the Program was met, on the back of a sustained structural adjustment effort since its onset. The external adjustment of the economy has been significant and faster than originally expected. Implementation of the structural reform agenda is also progressing in several fronts, namely in the areas of labor and product markets and the judicial system.

Following the successful completion of the bank capital augmentation exercise, including public capital injections, bank capitalization has significantly improved and banks' capital buffers remain adequate. The overall financing conditions have improved slightly but remain restrictive, in a context of high risk perception. Nonetheless, total credit to the economy remains resilient and overall consistent with the adjustment in the economy.

GDP is expected to fall by 1.8 percent in 2013 and grow by 0.8 percent in 2014. Inflationary pressures are projected to remain low. Export growth should remain robust, amidst continued market share gains.

Program implementation is progressing at a good pace but significant challenges and headwinds still lie ahead for the Portuguese economy. The adjustment needs to extend beyond the Program's duration and in line with its main pillars: structural reforms to increase potential growth, create jobs and improve competitiveness; fiscal consolidation; and safeguarding financial stability. Credible and consistent policies remain of the essence to safeguard prospects of a return to market financing.

San Marino: The international crisis has taken a toll on the economy of the Republic of San Marino and economic data show a negative trend. Unemployment stood at 8.5 percent in August 2013 and exports continue to contract. GDP is expected to fall by 3.5 percent in 2013, while state budget deficit was equal to about €27 million in 2012.

Against this background, the Government is implementing the interventions foreseen by its program in various sectors and aimed at budget rebalancing through the adoption of some measures, such as the tax reform that should enter into force starting from 2014. The planned reform aims at broadening the tax base and enhancing equity. It reorganizes the tax assessments system and maintains the tax rate for corporates unchanged, in order to guarantee the competitiveness of the country. The tax reform is coupled with a spending review which is the result of an in-depth study conducted in the first half of 2013, providing specific recommendations. Some expenditure cuts have already been made in the 2013 supplementary budget, while a systemic approach will result from structural reforms to be enacted in the following years. Furthermore, a law to attract FDI has already been passed with the objective of fostering growth while the reform of the labor market and the law on commerce will soon be included in the parliament agenda. Moreover, a feasibility study for the introduction of VAT is under way.

The relationship with Italy is expected to normalize soon. The 2002 double tax agreement, now including the Protocol of Amendment signed in 2012, entered into force on October 3, 2013. This will pave the way to the ratification of other two bilateral agreements on economic cooperation and financial cooperation and, by providing the legal basis for an effective exchange of information, will be considered as one of the main requirements that will be kept into account with respect to the position of San Marino in the so-called Italian "black list".

Worth mentioning is also a further reduction in the number of intermediaries operating in the banking and financial sector. With the current restructuring, intermediaries are seeking an operational dimension guaranteeing greater profitability, in full compliance with the law and supervisory provisions. Authorities are constantly monitoring this process; in this context, particularly important are the accurate assessments of the intermediaries' assets, as well as of the capital and liquidity profiles. Equally intense is the institutional activity supporting the strategic repositioning of the financial system in a context of integration with foreign markets. To this end, the alignment process to international standards has been brought forward, also in compliance with the provisions of the new monetary agreement signed with the European Union in 2012.

In this area, particularly important is San Marino access to SEPA as from February 2014, so as to guarantee the operation of the national payment system in the new context of European rules for retail payments.

Role of the IMF

Surveillance

Over the last six months, the Fund has further enlarged the scope of its multilateral surveillance and strengthened the risk and spillover analyses. These activities are instrumental to enhance crisis prevention and help provide more in-depth policy recommendations at both global, regional and country-levels. In this respect, further methodological developments and deeper analyses to address consistently bilateral and multilateral issues would be appropriate. It is also paramount to ensure the necessary coherence of the Fund policy advices provided in both the bilateral and multilateral surveillance as well as in the policy papers.

Low-Income Countries (LICs)

Many LICs showed significant resilience over the course of the global crisis. As a matter of fact, the 2009 reform of LICs facilities, through the latest adopted modifications (April 2013), has proved effective: in the first eight months of 2013 the demand for PRGT resources has been significantly lower than in the past. Also, we are pleased to note that monitoring developments in LICs has improved significantly: the latest report on Risks and Vulnerabilities in LICs has an innovative approach in two ways: the partition of LICs into four smaller homogeneous groups and the matching of different plausible shocks with possible policy reactions. This approach makes subsequent policy recommendations better tailored to specific circumstances, making the exercise more useful for policy purposes and, ultimately, for strengthening LICs' self-sustainability in the medium term.

Governance

The completion of the 14th General Review of Quotas by the implementation of the 2010 Quota and Governance Reforms remains a key objective. Considering the tight deadline of January 2014 agreed at political level, it is of the essence to deliver on our commitments, including the agreement on a quota formula within the context of the 15th General Review of Quotas. In this respect, a balanced and comprehensive package – that deals with all the issues in the quota formula - and a spirit of compromise by the whole membership are needed.