IMF EXECUTIVE BOARD DISCUSSION SUMMARY

The following remarks were made by the Chair at the conclusion of the Executive Board's discussion of the Fiscal Monitor, Global Financial Stability Report, *and* World Economic Outlook *on September 20, 2018.*

Executive Directors broadly shared the assessment of global economic prospects and risks. They observed that the global expansion, while remaining strong, has lost some momentum and growth may have plateaued in some major economies. Prospects increasingly diverge among countries, reflecting differences in policy stances and the combined impact of tighter financial conditions, rising trade barriers, higher oil prices, and increased geopolitical tensions. Beyond 2019, growth in most advanced economies is expected to be held back by slow labor force growth and weak labor productivity. In emerging market and developing economies, growth is projected to remain relatively robust, although income convergence toward advanced economy levels would likely be less favorable for countries undergoing substantial fiscal adjustment, economic transformation, or conflicts.

Directors generally agreed that near-term risks to the global outlook have recently shifted to the downside and some have partially materialized. Trade barriers have risen, with adverse consequences for investment and growth. Financial conditions in most emerging market and developing countries have tightened since mid-April. Capital flows to some of these countries have declined, reflecting weak fundamentals, higher political risks, and/or U.S. monetary policy normalization. While financial conditions in advanced economies remain broadly accommodative, an inflation surprise could lead to an abrupt tightening of monetary policy and to an intensification of market pressures across a broader range of countries. In addition, most Directors saw as key risks a further escalation of trade tensions, a rise in political and policy uncertainties, and growing inequality. Meanwhile, high debt levels limit the room for maneuver in many countries.

Most Directors considered that the recent intensification of trade tensions and the potential for further escalation pose a substantial risk to global growth and welfare. They noted that unilateral trade actions and retaliatory measures could disrupt global supply chains, weaken investor confidence, and undermine broader multilateral cooperation at a time when it is urgently needed to address shared challenges. They therefore urged all countries to adopt a cooperative approach to promote growth in goods and services trade, reduce trade costs, resolve disagreements without raising tariff and nontariff barriers, and modernize the rules-based multilateral trading system. The possibility of an outcome in which trade issues could be resolved in a positive way was also pointed out. Directors noted that persistent large external imbalances continue to call for sustained efforts, mindful of countries' cyclical positions, to increase domestic growth potential in surplus countries and to raise supply or rein in demand in deficit countries.

Given a narrowing window of opportunity, Directors underscored the urgency of policy measures to sustain the expansion, strengthen resilience, and raise medium-term growth prospects. They encouraged countries to rebuild fiscal buffers where needed, and implement growth-friendly measures calibrated to avoid procyclicality and the risk of sharp drags on activity. Directors agreed that, where inflation is below target, continued monetary accommodation remains appropriate. Where inflation is close to or above target, monetary support should be withdrawn in a gradual, data-dependent, and well-communicated manner. Directors emphasized the critical role of structural reforms in boosting potential output, ensuring that gains are widely shared, and improving safety nets—including to protect those vulnerable to structural change.

Most Directors shared the assessment that near-term risks to financial stability have increased while medium-term risks remain elevated. They highlighted, in particular, the buildup of financial vulnerabilities over the past few years of very accommodative financial conditions, including high and rising public and corporate debt,

and stretched asset valuations in some major markets. Addressing these vulnerabilities remains an important priority for many countries. For some countries, priorities include cleaning up bank balance sheets, improving corporate governance, and addressing risks from the sovereign-bank nexus, although a number of Directors felt that regulatory issues pertaining to sovereign exposures would best be left to the remit of the Basel Committee on Banking Supervision, which is the standard-setting body on the matter for a number of member countries. Directors also stressed the importance of completing and fully implementing the regulatory reform agenda, and of avoiding a rollback of reforms that have contributed to a more resilient financial system ten years after the global financial crisis.

Directors agreed that financial regulators and supervisors should remain vigilant about potential threats to financial stability and stand ready to act. They called for special attention to liquidity conditions and new risks, including those related to cybersecurity, financial technology, and other institutions or activities outside the perimeter of prudential regulation. These require policymakers to further develop policy tools, including macroprudential policies, and deploy them proactively as needed, as well as enhance coordination across borders.

Directors stressed that, as monetary policy normalization proceeds in advanced economies, emerging market and developing economies need to prepare for an environment of tighter financial conditions and higher volatility. Countries need to tackle their vulnerabilities and enhance resilience with an appropriate mix of fiscal, monetary, exchange rate, and prudential policies. In certain circumstances, capital flow management measures may be appropriate but not as a substitute for macroeconomic adjustment. Directors observed that markets have so far differentiated among emerging market and developing economies based on their fundamentals and idiosyncratic factors. In this context, they underlined the importance of maintaining credible policy and institutional frameworks, strengthening governance, and improving human and physical capital. Directors noted that the current environment highlights the need for the Fund to offer granular, tailored policy advice and stand ready to provide financial support to its members as needed.

Directors underscored that priorities for low-income developing countries include building resilience, lifting potential growth, improving inclusiveness, and making progress toward the 2030 Sustainable Development Goals, while commodity exporters should also prioritize economic diversification. Stronger efforts are needed to create room for development expenditure, through broadening the tax base, improving revenue administration, and prioritizing spending on health, education, and infrastructure, while cutting wasteful subsidies. Directors also called for urgent action to contain debt vulnerabilities, which are rising in many countries. They stressed that both debtors and creditors share a responsibility for ensuring sustainable financing practices and enhancing debt transparency.

Directors agreed that public sector balance sheet analysis provides a useful tool to analyze public finances. By revealing the full scale of public assets in addition to debt and nondebt liabilities, it helps governments identify risks and manage both assets and liabilities, potentially reducing borrowing costs and raising returns on assets. Directors noted that the long-term intertemporal analysis is particularly relevant in aging societies. They also saw the benefits of the added transparency in enriching the policy debate. At the same time, Directors acknowledged that the balance sheet approach still has limitations, notably data quality and differences in accounting practices hindering cross-country comparisons, and thus it should be used with caveats to complement traditional fiscal analysis.