International Monetary and Financial Committee

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**Statement by The Honourable James Michael Flaherty,
Minister of Finance, Department of Finance, Canada**

On behalf of Antigua and Barbuda, The Bahamas, Barbados, Belize, Canada, Dominica, Grenada, Ireland, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines

Statement Prepared for the International Monetary and Financial Committee of the Board of Governors of the International Monetary Fund

The Honourable Jim Flaherty, Minister of Finance for Canada,

on behalf of Antigua and Barbuda, the Bahamas, Barbados, Belize, Canada, Dominica, Grenada, Ireland, Jamaica, Saint Kitts and Nevis, Saint Lucia, and Saint Vincent and the Grenadines

Washington, DC, April 25, 2009

This meeting is taking place against the backdrop of the most synchronized global recession since the International Monetary Fund (IMF) was created 65 years ago. The credit crisis that originated in the financial systems of advanced members has radiated out to other Fund members, resulting in the contraction of credit, and sudden stops and reversals in capital flows. Moreover, the crisis has spread from the financial sector to the "real" economy as output, employment and trade volumes have fallen dramatically.

These effects have been felt by Fund members around the globe. In Canada, real GDP declined by 3.4 per cent in the fourth quarter of 2008 and current indicators point to a further sharp decline in the first quarter of 2009. The Government's Economic Action Plan, which was tabled in January, provides support to the Canadian economy over the next two years equivalent to 3.2 per cent of gross domestic product (GDP), including leverage from other levels of government. In addition, the Plan includes a $200-billion Extraordinary Financing Framework to improve access to financing for Canadian households and businesses. As a result, after a decline in Canadian real GDP of 2.5 per cent in 2009, the IMF expects a rebound in growth to 1.2 per cent in 2010—the strongest performance of any Group of Seven (G7) economy. This relative vigour reflects the sound policy frameworks and comparative strength of Canadian banks, which support credit flows and provide the foundation for a resumption of growth.

Ireland's economy is set to contract by 7.75 per cent this year as a combination of deteriorating domestic and external conditions weigh upon activity. In the recent supplementary budget, a number of revenue-raising measures and public expenditure cuts were implemented in order to limit the deterioration in the general government deficit to 10.75 per cent of GDP for 2009. In addition, to address the issue of asset quality in the banking system, the Government will establish on a statutory basis a National Asset Management Agency to which certain assets will be transferred from the banks. The purpose of this initiative will be to strengthen the banks' balance sheets and achieve a sustained flow of credit to the economy.

In our Caribbean constituencies, economic activity has decelerated: tourism, the region's major foreign exchange earner, has declined; similarly, remittances, a major contributor to the region's national income, are down; and there has been a substantial drop in foreign direct investment flows. While seeking to address these challenges, the region remains committed to implementing sound macroeconomic policies and reforms to strengthen the economic and financial architecture to reduce vulnerabilities and to build the necessary safeguards for the future. The role of the international financial institutions and other development partners remains critical in assisting the Caribbean region in implementing short- and long-term financial and macroeconomic policy responses to the crisis.

Some of our Caribbean countries have significant financial sector activities. There is a risk that changes to financial sector regulation in advanced countries could have negative unintended consequences on these activities. In particular, there is a risk that measures taken against non-cooperative jurisdictions, including tax havens, could have unintended negative impacts on well-regulated, transparent, financial centres. I believe that this should be avoided. Countries that comply with international standards should be protected from such measures.

The Global Recession and the International Response

The severity of the current downturn has naturally led to comparisons with earlier episodes of global economic contractions, particularly the Great Depression. The Fund was designed to assist its members to avoid the policy pitfalls that contributed to the prolonged economic stagnation of the 1930s: monetary policy did not provide liquidity in response to severe financial shocks; fiscal policy turned pro-cyclical as national economies started to contract; and trade protectionism exacerbated the downturn, turning a severe recession into a global depression.

We have learned from these policy failures. In the last six months, global leaders have agreed on the importance of taking concrete steps to quarantine impaired assets and recapitalize banks, where necessary; to implement fiscal and monetary stimulus as quickly as possible; to guard against protectionism in all of its forms; and to strengthen the financial system through sound national regulatory and supervisory frameworks and better international cooperation and surveillance.

Moreover, we have a set of institutions to promote international economic and financial cooperation. The IMF's mandate of promoting international monetary cooperation and global financial stability, which has facilitated the expansion of international trade, has never been more relevant.

Response to the Crisis

In London a few weeks ago, global leaders reaffirmed the central role of the IMF by agreeing to a number of measures to ensure that the Fund has the capacity to address the current crisis. These measures include:

- Negotiating temporary bilateral credit arrangements with the Fund totaling US$250 billion, of which Canada has agreed to provide US$10 billion.

- Expanding the New Arrangements to Borrow (NAB) by up to US$500 billion. Canada's proposed US$10-billion bilateral credit arrangement will be rolled into a new NAB commitment, increasing our stake in this important multilateral arrangement five-fold. We encourage other creditor members to follow suit, particularly those who are not currently NAB members.

- A general Special Drawing Right allocation equal to US$250 billion, which will quickly provide almost US$100 billion in reserve assets to emerging market and low-income countries.

- Doubling the IMF's concessional lending capacity for low-income countries in a manner that is consistent with debt sustainability.

- Implementing the 2008 quota agreement as quickly as possible, which will increase the IMF's quota resources by almost 12 per cent. Canada is completing the domestic steps required to ratify this agreement and I urge other IMF members to do the same.

- And, finally, completing the next review of IMF quotas by January 2011, accelerating the process by two years.

Reforms have also taken place at the IMF in response to this crisis, such as the development of the Flexible Credit Line for precautionary purposes. All of these efforts reflect the ongoing relevance of the IMF and demonstrate that the role of the institution will never be static.

The Changing Role of the IMF

As important as these measures are, it is clear that further concerted efforts are needed if the Fund is to play a stronger role in resolving this crisis and in preventing future ones. Prior to the current crisis, there were fundamental tensions among the membership with respect to the legitimacy, credibility and effectiveness of the Fund. These issues remain, notwithstanding the broad agreement on the continued importance of the Fund in assisting its members in the current crisis, and will have to be addressed to the satisfaction of the entire membership. Indeed, as IMF Governors, we have a collective responsibility to set a long-term course for the Fund. The upcoming quota review provides a unique opportunity to develop this common vision. A clear agreement on the IMF's role will ultimately help us to determine the resources and tools that it should have at its disposal, the responsibilities its members have to the institution and each other, and how it is best organized and governed.

The fundamental objective of the Fund remains the same—to promote international monetary cooperation and financial stability by assisting its members respond appropriately to external shocks through a judicious balance of financing and adjustment. And, yet, we have to recognize that, as a result of the remarkable process of financial integration that we have witnessed over the past two decades, the environment in which the Fund operates has changed. Our collective challenge is to ensure that the Fund is capable of fulfilling its mandate.

As a result, the quota review should consider a number of fundamental questions:

- *What are the appropriate tools and level of IMF resources required for effective short-term crisis response?* The present environment has revealed the difficulties in distinguishing between illiquidity and insolvency. In examining the IMF's role in providing liquidity to members, it is important that we determine whether we have the appropriate mechanisms to address sovereign insolvency cases in a timely and orderly fashion.

- *What responsibilities do IMF members have to the institution and to each other?* The IMF relies on the willingness of its members to participate in the surveillance of macroeconomic and macroprudential policies, such as through Article IV and Financial Sector Assessment Program reviews. We need to determine the extent of the liberties we, as Governors, are willing to give IMF management and staff in pursuit of their independent surveillance and advisory mandates.

- *For low-income countries (LICs), do we have the right balance between short- and medium-term support, to help countries respond to temporary shocks, and longer-term assistance to help LICs with entrenched macroeconomic and structural imbalances?*

Governance

The quota review also provides a good basis for parallel consideration of the appropriate governance structure for the IMF. We are pleased that, in London, governments agreed on the need for an open process for the selection of the Managing Director, a long-standing position held by Canada. Leaders also agreed to study IMF governance and ways to increase Governors' involvement in the institution. Reports from the eminent persons' committee, chaired by Trevor Manuel, and from the Independent Evaluation Office (IEO) provide valuable insights deserving of reflection.

Looking forward, key governance questions include:

- *How is the IMF best organized and governed?* We need to achieve an appropriate balance between respecting Fund independence and maintaining appropriate oversight.

- *What are the appropriate responsibilities of each level in the organization?* Consistent with recommendations of the IEO and the eminent persons' committee, there should also be a clear delineation of the roles and responsibilities of each level of decision maker (within a transparent accountability framework).

As a key element of the quota review, which should start as soon as possible after these Spring Meetings, it is incumbent upon Governors, the Board and the Staff to engage on these fundamental mandate and governance questions in a thoughtful, constructive and collegial manner.

Conclusion

The extraordinary responses of IMF members to the economic and financial crisis reaffirm the international community's determination not to repeat the errors of the Great Depression. Under the Managing Director's leadership, the Fund has played a critical role in mobilizing international efforts to limit the risks of a prolonged global slump. Our work is not over, however, and we must continue to work collectively and cooperatively to return the global economy to the path of sustained growth.

The past few months have demonstrated the critical importance of the IMF in promoting international coordination and providing crisis support. Canada remains committed to the underlying objectives of the Fund—to promote international monetary cooperation, financial stability and international trade—which are the foundations of global growth and wellsprings of prosperity for all. As we move towards the next quota review, of central interest to all members is ensuring that the IMF is able to fulfill its mandate of promoting the public good of international monetary and financial stability in an effective manner. This will require a pragmatic discussion of the role of the IMF and the instruments, resources and governance structure required to achieve its mandate.

The international community has demonstrated how it can effectively come together to respond to a crisis. We must show a similar degree of collaboration and commitment in ensuring the IMF is equipped to play a central role in the 21st-century global economy.