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Statement by Mr. Hoekstra
Kingdom of the Netherlands—Netherlands

On behalf of
Republic of Armenia, Belgium, Bosnia and Herzegovina, Bulgaria, Republic of Croatia, Cyprus, Georgia, Israel, Luxembourg, Former Yugoslav Republic of Macedonia, Republic of Moldova, Montenegro, Kingdom of the Netherlands—Netherlands, Romania, and Ukraine

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Global economic context, prospects and policies

Global Economy

- With expected growth of 3.7 percent in both 2018 and 2019, the global economy is expanding strongly. The expansion of the last few years has resulted in a sharp decline of unemployment rates since the height of the crisis. However, this momentum is expected to fade in the medium term as growth rates converge to their potential level and output gaps close. While the current expansion remains broad based, there has been some divergence since the spring. Especially some emerging market economies with weaker fundamentals (such as those with high FX-denominated debt, large and long-lasting current-account deficits and concerns about central bank independence) are experiencing increased volatility, exchange rate pressures and a setback in growth.
- In the medium term, slow labor productivity growth and the leveling off of labor supply growth due to ageing will weigh on the potential growth of many countries. Lower potential growth, combined with higher social welfare expenditures as a result of an ageing population, increases pressure on public finances. At the same time public debt levels are still elevated in many countries despite strong growth and low interest rates. In addition, protectionist policies jeopardize the outlook.
- As output gaps are closing and inflation is converging to targets, monetary policy is likely to gradually normalize. The Fed is raising policy rates and the ECB has reduced the monthly pace of the net asset purchases to €15 billion after September 2018 until the end of December 2018 and anticipates that, subject to incoming data confirming the medium-term inflation outlook, net purchases will then end.
- A risk of rising interest rates is that it increases debt servicing costs, which may reveal financial vulnerabilities. On the other hand, higher interest rates may deter unproductive investments and clear the way for the entry and growth of more productive firms. This would contribute to the diffusion of innovation and the efficient allocation of resources, and may increase productivity growth.

Policy mix

- Policymakers should take advantage of the ongoing economic expansion to raise potential growth prospects by implementing structural reforms and reducing legacy debt.
- There is no room for complacency and ample reason to step up reform efforts. Surveys such as the 2018 OECD Going for Growth show that the pace of structural reforms slowed since the crisis and remained modest in 2017. The current environment of high growth and low interest rates offers a window of opportunity to implement structural reforms, as some of the negative short term effects of reforms may be less painful during periods of economic expansion.
- Well-designed reform packages which include product market reforms, activating labor market policies, and the better linking of the eligible pension age to life expectancy will increase investment opportunities, competition, employment and potential growth both in the short- and long run. Other types of reforms, such as enhancing the efficiency of insolvency frameworks, shifting from bail-out to bail-in, facilitating the risk bearing of capital or equity investments and the relaxation of overly rigorous dismissal legislation will increase to the capacity to absorb

shocks. All such reforms, including fighting tax avoidance and -evasion, promote fairness and generate inclusive sustainable economic growth.

- Furthermore, debt levels – both public and private – are still above pre-crisis levels in many advanced and emerging economies, which may pose risks to the outlook. The failure to reduce legacy debts decreases the ability to respond to future shocks and increases vulnerabilities going forward. High debt levels in advanced economies might also give rise to financial instability risks when interest rates rise. Fiscal buffers should be rebuilt, not only to safeguard sustainable public finances over the long-term but also to create policy space for a next downturn. However, fiscal policy should clearly remain anchored within a strong policy framework that safeguards public finances' sustainability over the long term. Specifically for the euro area, fiscal policy should fully respect the rules of the EU Stability and Growth Pact.
- There is also scope to improve the composition of public spending. Public investments should be prioritized and directed towards areas which contribute to productivity growth in the medium term, such as education, innovation and infrastructure. To restrain inequality, the efficiency of expenditures on social welfare should be increased. Better targeting of transfers to the lowest income groups and unemployed could decrease inequality without raising the costs of social welfare.

<u>Multilateral Policy Response</u>

- Free trade and global economic integration under an open, rules-based multilateral trade system are significant drivers of global economic growth. They have led to rising living standards because they encourage specialization, spread innovation, help lift productivity, increase consumer choice and lower prices for consumers and producers alike.
- Protectionist policies have – on aggregate – negative consequences, especially in today's world of global value chains. The goal should therefore be to increase the welfare gains, for all parties, by strengthening the rules-based, multilateral trading system. We should work constructively to mutually reduce remaining trade and investment barriers. Trade and investment disagreements should be resolved without resorting to tariff and non-tariff barriers.
- At the same time, it should be recognized that trade liberalization and technological change have had redistributive effects within societies as production has shifted across sectors and regions. While governments should emphasize the major net benefits of trade, they should also address the adverse effects that liberalizing trade and technological development have had in some parts of society. Broad access to high quality education and lifelong learning, active labor market policies, as well as efficient redistribution can help to ensure that the benefits of trade and economic integration are shared widely and accrue to all. Addressing these concerns might also reduce support for inward-looking policies.

The Fund's role and institutional issues

<u>IMF Resources and quota</u>

- We support the work towards the completion of the 15th General Review of quotas. The Fund should remain a quota based institution as quotas underpin the Fund's finances, governance and risk management framework. The Fund should remain at the center of the Global Financial Safety Net. While it is difficult to determine the exact amount of required resources, quota should be sufficient to cover future IMF lending in normal circumstances and borrowed resources should serve as the second line of defense if tail risk scenarios materialize. During crises, the Fund resources are intended to play a catalytic role to mobilize other sources of finance, including official lending and private lending. The 15th quota review and the review of the quota formula should continue to be treated as an integrated package and be fully anchored in the relevant IMF bodies. We believe it is important that the prospect for a possible quota increase should be clarified first, before discussing the quota formula. The current quota formula captures dynamic developments in the world economy and is already delivering on the aim of increasing the Fund's representativeness and preserving its legitimacy, which is crucial to the Fund's surveillance and policy advice missions. The main variables of the quota formula should remain both GDP and openness, as these capture the role and mandate of the Fund best. In particular openness reflects the integration of countries in the global economy, in line with the Fund's mandate to promote international cooperation, economic integration and its increased focus on the effects of spillovers. We see no need for a change in the quota formula. We also think that concentration of voting power and its negative effect on legitimacy and governance of the Fund should be an integral part of the discussion.

<u>Conditionality review</u>

- The main objective of the conditionality review should be to assess the effectiveness of the Fund-supported programs and its conditionality framework. Conditionality is a key element of every program while it is generally perceived as a by-product of the financing part of the program. In our view both the financing part and the conditionality part of a program should be given priority.
- It is important that the Fund guidelines on conditionality are implemented consistently across the membership. Striking the right balance between country-specific measures and evenhanded treatment is paramount for ensuring country ownership and the successful implementation of the Fund's programs.
- The Fund's program-design should be based on realistic growth and debt projections. Realistic assumptions on economic growth and debt projections are a prerequisite for successful program implementation. The upcoming review should address the necessity of working towards sensible and time ambitious reform targets. Thereby taking into account political economy considerations, such as the electoral cycle, to further increase the success rate of reform implementation. We believe the review would benefit from the inclusion of an assessment of the risk of facility shopping between the different facilities provided by other International Organizations.

<u>Debt developments in Low Income Countries</u>

- We remain concerned about the substantial rise of public debt levels in low-income countries (LICs) in recent years. This increase in debt levels has been accompanied by a significant shift in public debt composition towards the private sector, which exposes LICs to further fiscal risks and debt vulnerabilities.
- We urge the Fund in collaboration with the World Bank to help countries contain public debt vulnerabilities, support measures to enhance debt transparency and promote sustainable lending practices by both lenders and debtors. Discussions on sound macro-economic policies, how to boost domestic revenues and use these resources for efficient public spending should be at the heart of an intensive policy dialogue with LICs, especially with those countries that currently do not have a financial arrangement with the Fund. This policy dialogue could be an assessment whether the current Fund policy on debt limits should be broadened.
- We encourage the Fund to provide a quantitative assessment of borrowing space in debt sustainability analyses for low income countries and to identify other ways to enhance the early warning capacity of the Fund. Important gaps remain in the available data on public and publicly guaranteed debt in LICs with too narrow coverage of public sector entities and public guarantees. On the one hand scaled up support for improving debt management capacity is needed in order to assist countries in monitoring and reporting debt. On the other hand the proliferation and change in composition of creditors poses severe challenges. A strong approach to step up the coordination efforts is needed to improve creditor information sharing and the lack of transparency. Reporting obligations for both debtor and public and private creditors should be broadened, which helps to tackle important data gaps.

<u>Compensation and benefits</u>

- We strongly support a comprehensive approach to review the Fund's compensation and benefits framework. We welcome the paper on the comprehensive compensation and benefits review (CCBR) of last July as a first step in developing a more modern, transparent, comparable and cost-effective framework. However the CCBR should include all elements related to remuneration and benefits. We encourage the Fund to be more ambitious and discuss all reform options. We would also like to stress that the CCBR is an important review that asks for stronger Board involvement in order to be successful. This review should ultimately contribute to strengthen the Fund as an agile, diverse, and inclusive employer.

Other initiatives

- We also look forward to the forthcoming Comprehensive Surveillance Review that should contribute to the strengthening of the Fund's core task of surveillance that enhance sound policies and crisis prevention. Surveillance should be holistic, evenhanded and maintain a comprehensive approach covering all key macro-economic aspects. At the same time, programs should be made country-specific as policies and institutional frameworks differ strongly across the membership. As the world faces new economic challenges, the Fund should develop expertise on emerging issues that are macro-critical such as climate change, corruption, inequality, and Fintech. These topics should be treated within the Fund's mandate and in cooperation with other International Financial Institutions.
- In its field of expertise, through surveillance and advice, we encourage the IMF to help the membership in reaching the objectives set in the Paris Climate Accord. The IMF should strengthen its analytical work assessing the impact of climate risk on the balance sheets of financial institutions.
- We support the Fintech agenda of the Fund in order to foster the benefits of Fintech, while, at the same time, mitigating the potential risks of technological innovation. This years' Constituency meeting main theme was about Fintech and the opportunities for improving development and financial inclusion.
- We also strongly support the Fund's increased attention on governance, in particular corruption, as this is a key element for many countries to achieve sustainable and inclusive growth.

Support for IMF members

- Bosnia and Herzegovina, Georgia, Moldova and Ukraine benefit from financial support from the Fund. The authorities continue to show strong commitment to implement ambitious reforms and country ownership. They deserve continued support from the Fund and the international community in achieving their program goals.