FM's Address during BRICS Finance Ministers Meeting

Date: **22.09.2011** Time: 1130 **hrs.** Venue: **IMF HQ 1, Board Room, 12th Floor**

Dear Colleagues,

We are meeting here at the time when global economic growth seems to be losing its momentum after about a year and half of fragile and uneven recovery. There are signs of economic and financial weaknesses in Europe and the US that threaten the global economic outlook. The robust and quick recovery in EMEs also seems to be running out of steam. It is important that at this juncture the BRICS countries have come together to discuss the implications and the possible policy responses to the emerging situation in the US and Europe and in doing so make an assessment around the following agenda points:-

- State of the global economy and current risks;
- Policy response in advanced economies and market reaction;
- BRICS policy response and coordination;
- BRICS Report

Which we shall discuss during the course of this meeting.

I suggest that in view of the time constraint all the agenda items may be taken up together.

Global economic growth seems to be decelerating recently with a downward revision in growth projections of both advanced and Emerging Market economies after about a year and half of fragile, uneven and multi--paced recovery. The weaknesses in major developed economies continue to be a drag on global recovery and poses risks for world economic stability. Despite the return to growth, unemployment levels in the United States remains at unacceptably elevated levels. With the near term growth prospects in both the US as well as in the European countries appears to be rather bleak, and according to experts, the chances of a double dip recession cannot be ruled out. In the euro zone, the indications are that drastic austerity measures might entail a recession without resolving their debt sustainability problem, and possibly also affect the growth prospects of other neighboring European economies. There is also a fear that Euro zone sovereign debt crisis could spread to some larger countries that are too big to be bailed out. The European banking system is also at risk on account of its exposure to peripheral sovereign bonds and cross holdings that make them vulnerable to contagion from assets not directly on their balance sheets. Growth in Japan also remains a source of concern following the after effects of the earthquake and tsunami.

3. It is therefore evident that the revival of the global economy following the financial crisis of 2008 has started to falter. Successive

numbers on growth, industrial production and forward looking indicators are suggestive of an impending recession in advanced economies. The most serious and immediate problem faced is the debt crisis in several advanced economies with the market perception that public debt of these countries could continue to rise even as growth remains subdued. Even under conservative assumptions, debt in relation to GDP will continue to rise and exceed the 100 per cent on an average for the next few years and many advanced economies will face large and increasing funding needs. While a spike in debt has always followed deep recessions, advanced economies have been able to grow their way out of high levels of debt in the past. However, the recent demographic changes make the growth prospects in several developed countries much more challenging. As and when interest rates rise, levels of public debt might become more and more unsustainable.

4. Corresponding to the rising public debt, the risk of enhanced financial fragility has also increased because public indebtedness has got intricately linked to the health of the banking sector. There is risk that the debt of these two parties will feed into one another and form a vicious circle and amplify the risk throughout the world. Markets seems to be speculating that while Sovereigns could bail out the financial sector, the only way sovereigns can be bailed out is through higher

quantitative easing that is likely to eventually result in inflationary outcomes.

5. Currency markets are also being impacted due to investors seeking safer havens. The consequences has been increased volatility of capital flows, and heightened prices of safe haven assets like gold, US Treasuries and also commodities. The deleterious effects that these developments would have on the global economy are issues of concern.

The advanced economies, most notably the US, has had to keep in place a policy of aggressive fiscal stimulus and cheap money for an extended period in their effort to help the financial sector's return to normalcy and to stimulate economic activity. However unusually low interest rates and two rounds of quantitative easing in the US have so far has not resulted in a sustainable revival of the real economy. On the contrary, it had added new risks, including greater volatility among major currencies and commodities, and a surge of volatile capital flows to emerging markets. Measures taken from time to time in the euro zone to deal with the crisis emanating from the peripheral economies have also not been successful in stabilizing the situation and reassuring the markets. What is adding to the market nervousness is perhaps the apparent lack of confidence in the ability of policy makers to adequately handle a possible "double dip" since both fiscal and monetary tools seem to be exhausted. Another major risk factor is that any rise in protectionist tendencies as a knee-jerk reaction to persistently high levels of unemployment in advanced countries would further worsen the economic sentiments and the growth prospects of the EMEs and indeed the rest of the world.

In key advanced economies, the necessary hand-off from public to private demand is not taking place. The fundamental problem is that weak growth and weak balance sheets of governments, financial institutions, and households are feeding negatively on each other. If growth continues to lose momentum, balance sheet problems will worsen, fiscal sustainability will be threatened, and the scope for policies to salvage the recovery will disappear.

An area of major concern is that financial markets continue to be in state of uncertainty showing little confidence in the growth prospects and policy actions taken by sovereign governments particularly in advanced markets. As I had said previously, the most serious problem faced on an immediate basis is the market perception that public debt of developed countries will continue to rise even as growth remains subdued. The downgrading of US sovereign long-term debt by Standard and Poor's, is nevertheless a clear indication of a lack of conviction about policy action. The fall in several global forward looking indices also reflects in some ways a similar sentiment.

The BRICS economies have been key drivers of the global recovery, but even their growth is faced with the challenge of inflation and continuing uncertainty in global financial markets. The volatility in capital flows arising from policy choices is a further source of vulnerability.

I would like to have your views and concerns on the global economy and current risks we face. Some of the questions that need to be addressed are:

- How should policy response be coordinated at the international level, especially since global economic cycles seem to be divergent;
- What, if any, should be the role of the IMF and other IOs in ensuring that the world transits more smoothly through the current turmoil?
- What steps BRICS can take in the current situation.

Now taking up the last agenda item, I would like to recap our earlier resolve at the London meeting on September 4, 2009 to commission a study by our Finance Ministries and Central Banks regarding where the world economy will be heading in the near future and the role of the BRIC countries. Given the fact that the emerging markets of Brazil, Russia, India, China and South Africa would come to play a dominant role in the global economy, it will be important for the group to explore the role of the BRICS countries in the face of the emerging global challenges and identify areas of cooperation and synergies between BRICS countries for promoting mutual growth and collectively harnessing the global economic recovery. We expect that the global community that has so far looked at BRICS from the viewpoint of investment bankers, would be interested to get the BRICS's own perspective of their role in the global economy.

India offered to Anchor this report. I am glad to inform you that recently a workshop was held in New Delhi wherein experts from Finance Ministries and Central Banks discussed and provisionally finalised the study. I am happy to share the third draft report in this regard and would simultaneously call on our experts from Finance Ministries and Central Banks to finalise this report at the earliest and present the final report before our next meeting as a group.

Thank You.

BRICS Finance Ministers' Joint Communiqué issued at the end of Meeting
Washington, September 22, 2011

We, the BRICS Finance Ministers and Central Bank Governors, met on September 22, 2011 in Washington DC, USA, amid growing concern regarding the state of the global economy.

While BRICS countries recovered quickly from the 2008-09 global financial crisis, some of us have been subject to inflationary pressures and growth prospects of all our countries have been dampened by global market instability. In advanced countries, the build up of sovereign debt and concerns regarding medium to long-term plans of fiscal adjustment are creating an uncertain environment for global growth. Also, excessive liquidity from aggressive policy actions taken by central banks to stabilize their domestic economies has been spilling over into emerging market economies, fostering excessive volatility in capital flows and commodity prices.

The immediate problem at hand is to get growth back on track in developed countries. In this context we welcome the recent fiscal package announced by USA as well as the decisions taken by Euro area countries to address financial tensions, notably by making the EFSF flexible. It is critical for advanced economies to adopt responsible macroeconomic and financial policies, avoid creating excessive global liquidity and undertake structural reforms to lift growth create jobs and reduce imbalances.

. The current situation requires decisive actions. We are taking necessary steps to secure economic growth, maintain financial stability and contain inflation. We are also determined to speed up structural reform to sustain strong growth which would advance development and poverty reduction at home and benefit global growth and rebalancing. The contribution of BRICS countries and other emerging market economies to global growth is rising and will increase further. However, global rebalancing will take time and its impact may not be felt sufficiently in the short-term. We will also work to intensify trade and investment flows among our countries to build upon our synergies.

The BRICS are open to consider making additional efforts in working with other countries and International Financial Institutions in order to address the present challenges to global financial stability, depending on individual country circumstances.

We are concerned with the slow pace of quota and governance reforms in the IMF. The implementation of the 2010 reform is lagging. We must also move ahead with the comprehensive review of the quota formula by January 2013 and the completion of the next review of quotas by January 2014. This is needed to increase the legitimacy and effectiveness of the Fund. We reiterate our support for measures to protect the voice and representation of the IMF's poorest members. We call on the IMF to make its surveillance more integrated and evenhanded.

Multilateral Development Banks are considered by developing countries as important partners in helping them meet their long term development finance needs. In the current global economic environment, the Banks need to mobilize more resources to increase their assistance to low income and other developing countries including finding ways of expanding their lending capacity, so that development finance is not neglected.

In the face of a slowdown of global economic growth, it is necessary to maintain international policy co-operation and co-ordination. We remain committed to work with the international community, including making contributions to the G20 Cannes Action Plan consistent with national policy frameworks to ensure strong, sustainable and balanced growth. We shall work together in searching for a coordinated solution to the current challenges as we did in 2008-09.