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GRAY/21/2026

July 14, 2021

**Statement by Mr. Huh, Mr. Yoo, and Mr. Becker on 2021 External Sector Report
(Preliminary)
Executive Board Meeting
July 16, 2021**

The External Sector Report is a key surveillance instrument for the IMF membership and is a useful tool in redressing imbalances that inhibit the best functioning of the international monetary system. We broadly agree with staff findings in the report at a time when such analysis is further complicated by the extraordinary health crisis. We wish to highlight some key issues.

It is encouraging to note the main conclusion that underlying global imbalances, taking desirable domestic medium-term policies and temporary adjustments due to the COVID shock into account, were broadly unchanged in 2020. The widening of global current account balances without adjustments is found to mainly reflect the impact of the COVID crisis on travel, oil, medical goods, and the composition of household consumption. This widening contrasts with developments in past recessions, during which global balances narrowed. It may imply that since the initial turmoil in 2020, larger fluctuations in current account balances are in part the result of exceptional policy support. Therefore, it is worthwhile to emphasize analysis of ‘excessive’ current account imbalances rather than the ‘headline’ measure.

We see adjustments to the External Balance Assessment (EBA) as appropriate to separate out transitory, sector-specific factors of the current crisis. *We wonder about the possible structural breaks in the interaction between the variables in question during major global shocks like the Asian Financial Crisis, the Global Financial Crisis, and the COVID pandemic.* It is instructive to note that the estimated adjustment factors account for about two-thirds of the movement of current account balances for major economies. As there is high uncertainty regarding the path of the pandemic, similar adjustments to the EBA may be needed in future reports. Therefore, we lend our support for staff to monitor developments and refine the methodology where necessary.

We welcome that the impact of the COVID-pandemic on tourism and remittances was quantified, as it is very important for our members in Asia and the Pacific (some of which are not ESR countries). The adjustments made provide a better depiction of underlying external balances and

it is useful for policy makers to see that the tourism-dependent countries in the region are some of the most affected in the world.

We agree with the overall theoretical expectation that capital should flow downhill from rich advanced to lower-income emerging economies but note that there are important exceptions. In some cases, advanced economies have highly productive investment projects in infrastructure and resources that draw on the pool of global saving. For less advanced economies, domestic institutional and structural reform is important to ensure that capital can flow unobstructed downhill from advanced saving economies.

It would have been good to see a somewhat deeper analysis of gross trade flows rather than the strong focus on the net current account balance, given that there were partially offsetting movements in gross exports and gross imports. This is of interest because even though in the current episode the current account balance did not move by as much as in an asynchronous recession, the gross movements are nonetheless associated with a very severe and costly shock.

The extensive discussion and analysis of the link between fiscal policy and the current account is very helpful. This is especially so in the context of how current imbalances are likely to evolve in the consolidation phase after the crisis. One interesting way to assess imbalances attributable to fiscal expansion in 2020 would have been to compare them to a ‘no-policy-response’ baseline which would have presumably resulted in a much deeper recession and associated costs. Implicitly, policy makers chose to take on the imbalances associated with the policies currently in place to avoid the costs and imbalances of not responding as they did. *Regarding the empirical analysis and model simulation in Chapter 2—showing the impact of fiscal consolidation—we wonder about the meaning of “growth enhancing fiscal consolidation” which is used frequently.*

We fully agree that ensuring a sustainable global recovery and preventing long-term scarring from the crisis is the policy priority. Promoting external rebalancing is also important through growth-oriented fiscal policy by adopting greater public sector investment in digitalization, infrastructure, and green transition.

It is important to address trade and technology tensions. We would have preferred more emphasis and coverage of this issue in the report. Imbalances are not a valid reason for protectionism, but rather a strong case for reinforcing the multilateral rules-based trading system, including a well-functioning WTO dispute settlement system. We remain concerned over currency-based countervailing duties as they would pose a significant risk to the multilateral trade and international monetary systems, and also be counterproductive to the country adopting such measures.

We believe that in the medium term, carefully calibrated policies are needed to achieve domestic objectives while contributing to external rebalancing. Recommendations regarding the macroeconomic policy mix should also take into account the cyclical context and avoid premature fiscal consolidation until the economy firmly recovers. Structural reforms have a role in addressing external imbalances, but policy advice has most traction when it is clearly centered on domestic objectives—as implementation challenges often stem from domestic political economy constraints. In

an environment of elevated uncertainty, the bias should be toward allowing flexibility to make the necessary adjustments as efficiently as possible.