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**Statement by Mr. Alazzaz on Seminar--Reserve Accumulation and International
Monetary Stability
(Preliminary)
Executive Board Seminar 10/2
May 28, 2010**

I thank staff for an informative paper on reserve accumulation and international monetary stability for today's seminar, which brings together a number of reform ideas on the functioning of the international monetary system (IMS). It has been noted in the paper that the last comprehensive discussion of reform of the IMS was held nearly four decades ago. This should be seen as an evidence of the resilience of the current IMS over decades. In this context, it has rightly been observed that the global crisis of 2008/09, for all its costs, has not jeopardized international monetary stability, and the IMS is not on the verge of collapse. Against this background, it would be difficult to agree on major reforms, especially as there is no obvious path to a more robust system and many of the ideas presented in the paper would entail a number of complex forms of international collaboration.

As regards the imperfections in the current system, large and volatile capital flows do create significant complications for macroeconomic management as "floods" and "sudden stops" have become a frequent feature of financial globalization. In this regard, it has rightly been noted in the paper that "booming capital inflows can fuel asset bubbles, poor resource allocation, and balance sheet risks when lending is in foreign currencies". On the other hand, "the potential for rapid outflows-and the associated liquidity shocks-have created a strong need for insurance". In this connection, while there are no easy solutions, the forthcoming discussion on the Fund's role in capital flows should provide an opportunity to look at various options to help reduce capital flow volatility.

On reserve accumulation, I fully endorse the view expressed by staff that accumulation for structural reasons, e.g., large public savings to ensure intergenerational equity given an eventual depletion of an oil endowment, does not call for policy adjustment. Indeed, surpluses in oil-exporting countries are different in nature from those of other countries as they are a result of exports of non-renewable resources to meet global demand. Therefore, it

is critical to use these surpluses effectively to raise the growth potential of the economy and accumulate savings to help ensure intergenerational equity and smooth out fluctuations in revenue in the period ahead.

Still on reserve accumulation, the experience during the recent crisis has clearly shown that emerging market countries with improved policy fundamentals and large reserves have generally fared better. It is therefore important to encourage countries to self-insure firstly through prudent policies and secondly through maintaining adequate buffers against shocks (i.e. reserves). While accumulating reserves is not costless, there are substantial benefits to such accumulation that go beyond reducing vulnerability to shocks. With regard to the idea of penalties such as a reserve requirement on “excess” reserves or an automatic tax on persistent current account imbalances beyond a certain threshold, staff have rightly raised doubts about the feasibility of introducing such penalties.

On the supply side, global reserves are diversified to some degree and further diversification is likely to continue gradually over time. However, there are no currently available candidates that can match the size of the U.S. economy or the depth and liquidity of its financial markets, although the transition to a truly multi-polar reserve system could emerge over time. Moreover, as recognized in the paper, it is not clear whether a more diversified reserve system, in net terms, would be an improvement over the current system. On the possible Fund’s role in encouraging the orderly emergence of a diversified system, I remain of the view that the reserve composition is reflective of the needs and preferences of member countries. I therefore do not support the suggestion in the paper that members should be required to report their reserve composition to the Fund, including information on reserve holder’s benchmark for the currency composition of reserves.