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

We would like to thank the staff for preparing a paper that enumerates a wide variety of measures to improve the stability and robustness of the international monetary system.

The underlying circumstances of today's world economy have greatly changed from those in the 1940s when the Fund was established, or those in the 1970s when the international monetary system was reconstructed from scratch. Given the recent market volatility and developments since the outbreak of the global financial crisis in October 2009, it is hard to foretell even short-term developments in the international monetary system.

While the Staff Paper tries to include many "old ideas" that have long been discussed, this approach gives us the impression that the discussion runs the risk of turning out to be excessively hypothetical, or superficial, by paying less attention to the actual differences in the underlying economic and financial environment between today and the periods when these old ideas were originally proposed.

Against this background, for the time being, rather than refloating overly innovative or archaic ideas, it seems more productive to place the focus of our primary attention upon the discussion of building a resilient and credible global financial safety net (GFSN) that will curtail the risks associated with the volatility of capital flows.

Adequacy of the Size of the Reserve Accumulation

Under the current circumstances, in which many fast-growing emerging market countries still face the potential risk of a sudden reversal of capital flows, utmost attention should be paid not to conduct a purely conceptual analysis without a balanced viewpoint with regard to reserve accumulation. Although the staff proposes that the Fund, for self-insurance purposes, create guidelines to assess the adequacy of the size of a country's reserve accumulation; in practice, it seems almost impossible to completely distinguish reserve accumulation for self-insurance purposes from that motivated by other policy purposes. Also, the size of the

reserve accumulation would vary not only in relation to its objective, but also depending on other factors, such as: an individual country's level of domestic savings and its perception of risks, costs, and the benefits of the reserve accumulation. Hence, even if the Fund were to establish such guidelines, it might, in fact, find no applicable cases.

A broad consensus seems to be emerging regarding the importance of establishing the GFSN. In this regard, further work needs to be done with respect to identifying: i) the specific features that are needed under today's circumstances (rather than those needed in the period of the Asian crisis), and ii) the ways to make the GFSN actually function as envisaged. In addition, it should be noted that it is difficult to persuade emerging market economies to reduce their reserve accumulation only on the grounds of the establishment of the GFSN.

As for advanced economies, the implications of accumulating reserves need to be examined from different perspectives. Indeed, in advanced economies, the opportunity cost of holding reserves seems to receive relatively small attention because, in advanced and mature economies, there are limited investment opportunities to acquire high returns. Rather, in advanced economies, this issue seems to be discussed primarily within the broader context of political debates, such as the appropriate size of the public sector's balance sheets, or identifying effective ways to hold the government accountable for its management of public assets.

Diversification of Reserve Assets

While the Staff Paper assumes that promoting the diversification of reserve assets will contribute toward building a more stable international monetary system, we are skeptical about this assumption, because the possibility exists that a move to the multi-polar system could exacerbate foreign exchange fluctuations and capital flow volatility, thereby making the international monetary system more unstable.

In addition, utmost attention should be paid to the possibility that deliberately diversifying reserve currencies could cause speculation in foreign exchange markets and destabilize, rather than stabilize, the international monetary system.