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Statement by Mr. Buisse, Mr. Rozan, and Ms. Albert on 2020 External Sector Report (Preliminary)
Executive Board Meeting
July 24, 2020

We strongly support the External Sector Report exercise, which lies at the core of the Fund's multilateral surveillance mandate. This ESR once again shows the persistence of excess global imbalances in 2019, about 40 percent of current account imbalances, with larger than warranted current account balances in the euro area. We understand the difficulty to integrate a comprehensive analysis of the Covid-19 crisis due to the lack of data and uncertainty surrounding the consequences of the crisis, but we consider that this challenge has been well tackled in the report, with useful insight. Nevertheless**, we would like to highlight that the main value added of the ESR is its structural dimension, and remains our central point of attention. At the current juncture,** this tool is particularly relevant as it can contribute to defining the optimal policy design for a strong, sustainable and balanced recovery. Indeed, most of the past recommendations would undoubtedly remain highly relevant to reduce excessive imbalances and prevent the building of new ones, while boosting an inclusive and sustainable growth.

Assessments and recommendations

We generally share staff's assessment of the global imbalances, but consider that uncertainty about their evolution is high. While imbalances could be slightly reduced next year, mainly because of the huge global demand shock and some offsetting effects between surplus and deficit countries, uncertainty is significant regarding the evolution of savings, and we would like to highlight the risk of an asymmetric adjustment as the one that took place in 2009. We thank staff for their valuable insights about remittances, tourism and commodities, which are key transmission channels of the crisis on the current account. Regarding the useful Boxes 1.4 and 1.5, we feel that the role of the monetary policies in the advanced economies could have been taken into account more explicitly, as well as the non-conventional policies in the emerging countries which contributed to stabilize their external situation. This could also help to elaborate more precise policies recommendations.

Regarding euro area, we note that while aggregate imbalances are moderate at most, significant imbalances persist for some members, both in flow and stock terms. The regional analysis could however have been more granular as country trajectories are heterogeneous, and it would be interesting to better understand the factors underlying the continuation of these diverging trends in 2020. Moreover, it's important to underline that the REER in the area is broadly in line with fundamentals. More specifically, **regarding countries assessments,** we note that if France external position is now in the category of a moderate weaker position than the level implied by medium-term fundamentals and desirable policies, it is due to a very marginal step over the 1 percent threshold, with a current account gap of -1.1 percent of GDP. Germany, Netherlands and Singapore continued to have a substantially stronger external position. Switzerland current account norm has evolved, and the country has now a moderately stronger position, from a broadly in line one last year. We also note several total staff adjustments, in particular: for Brazil, the adjustment about -0.5 percent due to NIIP considerations last year disappeared this year and the position has changed category from broadly in line to moderately weaker, for Mexico the adjustment increased by 0.6 from zero last year because of trade diversion, for Netherlands the significant adjustment increased from -1.5 to -2.3 percent due to new measurement biases. *Could staff provide more detailed explanation on these adjustments?*

Regarding the policy recommendations, we would like to insist on the need to not water down the Fund message on fighting excessive imbalances and to focus on structural recommendations to build the recovery. Indeed, vulnerabilities linked to excessive global imbalances worsen the effects of the crisis, and avoiding a worsening of these imbalances post crisis should remain a top priority. We are therefore not fully convinced by the short term/long term distinction this year, which has been preferred to last year's fiscal/monetary/structural categorization. Indeed, the short-term recommendations are broadly similar among countries, and while we are fully aware of the difficulty to assess hysteresis effects during these challenging times, most of the structural recommendations will remain valid to address global imbalances in the longer term. We would have also appreciated more granularity and tailored policy advice on structural recommendations, which could help to build a sustainable recovery. We fully agree with staff recommendations on the need for growth friendly fiscal measures, and to conduct fiscal consolidation once recovery is firmly entrenched, as well as productivity-enhancing measures in countries with excessive current account deficits. Regarding the United States, which mainly explain the global deficit, we would like to insist on structural policies to strongly support the working poor, increase human capital, improve competitiveness, and facilitate the transition to a lower-carbon economy. Relevant public and human capital investment, as well as an expansion of social safety nets in excessive surplus economies, in particular with significant fiscal space, such as Germany and the Netherlands, are also paramount, and could play a key role to boost the global recovery. Moreover, China's position remained in line with fundamentals and desirable policies, which we welcome, but still persisting internal imbalances indicate the necessity to continue to reform the SOEs, control credit evolution, ensure a robust financial system, and enhance social safety nets which is even more important with the current crisis. Finally, we fully share the need to avoid protectionist measures and countervailing duties based on exchange rate assessment, and we reiterate our message to promote a multilateral rules-based system to avoid negative impacts on our economies. We also support the ESR's call to modernize the multilateral rules-based trading system and restore a well-functioning WTO dispute settlement system.

NIIP

We found chapter 2 very interesting and the results should be disseminated and promoted in global multilateral forums. Significant progress on the NIIP topic has been made since last year, which helps bring another perspective for creditors. The chapter usefully recalls the evolution of determinants of external stress episodes over time (weak reserves, then excessive current account deficits and now external debt, in particular denominated in foreign currency). We found instructive the disentanglement of the valuation effects, which shows a weak role of the exchange rate movements and a key role of assets prices. There is also a clear asymmetry between advanced and emerging G20 economies with most of the emerging economies bearing a high risk on the liability side while taking very little risk on their asset side. It could be interesting to analyze more the financial risk on the assets side, regarding the asymmetric composition of debtors and creditors countries which leads to marked asymmetry in risk-taking. Moreover, we are wondering to which extent the abundant liquidity, which favors overvalued asset prices, has an impact on global imbalances. *What is staff view on this topic?*

Nevertheless, we are not comfortable with the treatment of precautionary and non-disbursing arrangements in the chapter, which risks undermining the Fund's overarching message on precautionary arrangements. We urge staff to revise the chapter before publication. It is problematic to describe application for a precautionary or non-disbursing arrangement as a "stress event". Precautionary facilities are an endorsement of strong policy frameworks, seeking to boost confidence and aiming to avoid a crisis, not representing one. Including non-disbursing arrangements in the stress sample is also problematic, as it distorts the sample by excluding countries which have chosen not to apply for a precautionary arrangement (instead pursuing less desirable and/or less proactive policies), as well as countries with weaker policy frameworks who do not meet the qualification criteria.

EBA methodology

We encourage staff to continue to work on structural changes which could affect the global imbalances. Work on the potential hysteresis effects of the crisis and their impact on global imbalances, with a new assessment of current account norms and REER equilibrium value, as well as the potential adjustment of recommendations, will be essential. Moreover, while GVCs seem to be more a resilience factor, the renationalization of supply chains may not necessarily increase the resilience of GDP to pandemics. We encourage staff to understand better potential GVC transformations. Moreover, the crisis could change behavioral consumption patterns, and evolution of savings and more specifically precautionary savings is unclear, and it could be interesting to see more analysis on this issue. *Could staff provide their view regarding the future evolution of the corporate, households and government savings?*

Many interesting areas of work were presented last year, and we strongly encourage staff to further explore these issues. The work regarding corporate savings, the role of MNEs and profit shifting seemed to be very promising, as well as a deeper understanding on the between inequalities and global imbalances. While we understand that the crisis changed the work agenda in the short run, we are looking forward seeing a deeper analysis whenever possible.