Press Information Bureau, Government of India
Prime Minister's Office 02-April, 2009 16:4 IST

PM's remarks at the official dinner hosted by Prime Minister Gordon Brown on the occasion of the G-20 meeting

Following is the text of the Prime Minister, Dr. Manmohan Singh's remarks at the official dinner hosted by Prime Minister Gordon Brown on the occasion of the G-20 meeting at London on 1st April, 2009:

"I would like to begin by thanking Prime Minister Gordon Brown and the Government of the UK for the warm welcome we have received and for the excellent arrangements made for the meeting. I would also like to welcome President Barack Obama to his first meeting of this Group.

The problems facing the world economy are well known and need no elaboration. The only point to note is that the downturn is much deeper than we though when we met in Washington D.C. in November last year, and the prospects of a recovery have receded to 2010 at best. This is the worst recession in sixty years and is generating negative expectations which threaten a downward spiral if not corrected. The pain is being felt both in industrialised countries and in developing countries.

A global crisis requires global solutions. In Washington D.C. we pledged to take action to revive the world economy and also to bring about basic reform of the financial sector to reduce the likelihood of similar severe crises in future and to build institutions that can intervene more effectively if we do. We have made considerable progress in several areas, but I believe much more needs to be done.

The world is looking to us to show that we can act cooperatively in a manner commensurate with the scale of the crisis. As we deal with the immediate problems, we must also be careful not to sacrifice the gains of openness of trade, direct investment and immigration. It will be a test of the leadership of the G-20 whether we can craft a strategy that meets all these objectives.

There can be no doubt that restoration of the banking system in the industrialised countries to full functionality is precondition for successful revival of the global economy. This is primarily a task for the Governments of the individual countries concerned. It is a task that will require commitment of resources on an unprecedented scale. The IMF has estimated that the write down of toxic assets needed may be as high as $2.8 trillion in the US and $1.4 trillion in Europe and Japan. Many Governments, most recently the United States, have made large commitments of resources to deal with the problem of tainted assets and also to recapitalise the banking system. More may well be needed.

A rescue effort on this scale will place a huge burden on tax payers and this has given rise to considerable public anger, which is entirely understandable. However, it has to be explained to tax payers, and also their elected representatives, that anger at the irresponsible, and even morally reprehensible behaviour on the part of managements of financial institutions, should not come in the way of efforts to resurrect the system.

I recognise that this is ultimately a political problem that has to be handled by each national government. This Summit can help by sending a clear message that the problem affects many industrialised countries and has to be tackled if we want to bring about an economic revival and tackle unemployment. The main reason why we can expect to avoid a repeat of the Great Depression is that governments know a great deal more about the role of contra-cyclical policies and they are also willing to act. However, contra-cyclical policies will not have their full expansionary effect if credit does not flow to where it should. We have to explain to the public that reviving the banks is important not for the banks, as is sometimes perceived by the public, but for the economy, for employment, and for global prosperity generally.

Active contra-cyclical policy must be a priority item on our agenda and global markets are looking to see if we are united on this issue. We have seen a massive contraction in consumer demand in industrialised countries arising from the wealth effect of the decline in house prices and in stock market values. This is compounded by uncertainty about future employment prospects. The emergence of excess capacity in several sectors is bound to discourage private investment. Some contraction of demand in countries where current account deficits were too high was to be expected. Ideally this should have been offset by expansion in surplus countries. For whatever reason, this orderly adjustment could not be brought about. We are now seeing a contraction that has overshot and contra cyclical stimulus is therefore necessary in all countries.

Most industrialised countries, and also developing countries, have responded by using monetary policy fairly aggressively to counter the downturn. They have also resorted to a fiscal stimulus to varying degress. I recognise that it is not easy to determine the level of fiscal stimulus that is appropriate for different countries in different circumstances. But we do know that expansionary policies are most effective when they are coordinated. I hope the Summit will give a clear signal that we are willing to act in a coordinated, or at least in a credible concerted manner, to ensure that the downslide is minimised.

The International Monetary Fund had estimated that a discretionary fiscal stimulus of about 2 per cent of GDP in 2009 would be needed, in addition to the operation of automatic stabilisers. This was to be followed by a similar order of stimulus in 2010 to achieve the objective of moving from an unavoidable decline of around 1% in 2009 to a modest positive growth of about 2% in 2010.

Available information suggests that whereas the actual stimulus of the G-20 countries in 2009 is approximately equal to the Fund target, what is currently planned for 2010 may be too little. Many observers have also commented that the modest global recovery projected for 2010 may be over optimistic. I recognise that there are time lags in the system and the effects of actions already taken may be felt only in the coming months, but it does seem that the risks lie in doing too little rather than too much, and we are not doing enough to ensure recovery in 2010.

If we cannot agree to do more, we should at least send a clear message that we will watch developments carefully in 2009 and act speedily to do more if necessary. The IMF should be tasked with monitoring developments in this area and reporting back periodically.

Let me now turn to the steps needed to ensure the revival of growth in the developing countries. These countries have suffered a double shock. They have seen a collapse in world trade, with an unprecedented decline of almost 9 per cent in trade volume in 2009. They have also suffered a massive decline of private capital flows estimated by the Institute of International Finance at close to $700 billion in 2009, with little prospect of a significant revival in 2010. To some extent, financial protectionism, built into the conditions for assisting banks in industrialised countries, may have encouraged this trend, though there are of course many other factors.

We in India have been fortunate in having weathered the global downturn better than many others. Our growth rate, which was close to 9% in the previous 5 years, will fall below 7% in 2008-09. Like other countries, we have made aggressive use of both monetary and fiscal policy, with a total fiscal stimulus or expansion of the fiscal deficit above the planned level of almost 4 percentage points of GDP in 2008-09. We hope to be able to achieve a similar growth rate in 2009-10, with continuing reliance on monetary and fiscal policy. We recognise the importance of fiscal sustainability and it is our firm intention to return to a fiscally sustainable path after 2010. The additional fiscal stimulus we have undertaken will raise our debt to GDP ratio by a few percentage points above what it would otherwise have been, but this is relatively modest compared to what would have happened had our banks suffered a financial crisis. Effective regulation of the banking system has gained us much more than any additional strain imposed by temporary fiscal expansion. Besides, since most of the fiscal stimulus will be directed to increased investment in infrastructure, it will in the medium term contribute to growth and thus help reduce the debt ratio automatically.

Expansionary policy at home in an environment where exports are weak and private capital flows have dried up would normally lead to pressure on the balance of payments. In our case this has been partly offset by the fall in oil prices, but even so, India's current account deficit in 2009-10, is likely to be about 1.4. per cent of GDP. We expect to be able to finance this without difficulty and in any case our strong foreign exchange reserves position enables us to cope with any shortfall in capital flows we may experience.

While India will be able to manage, many other developing countries may not be in the same position and this is where the international community can help. We must ensure that countries hurt by the massive withdrawal of private capital that has taken place, which is unlikely to be reversed in 2010, are able to rely upon an increased flow of resources from the international financial institutions. This will help these countries to maintain a higher level of demand than would otherwise be possible and thus help global revival.

There are several steps we can take which will demonstrate our willingness to help.

We must declare our resolve to increase the resources available with the IMF substantially, by around $500 billion over the next two years. This can be done initially through bilateral arrangements, an expansion of the NAB and other borrowing by the Fund. However, we should also signal that these are interim steps pending an increase in Fund quotas. The next quota review, normally due in 2013, should be advanced as much as possible, and we should aim at a doubling of IMF quotas at the very least.

In addition to increasing resources with the IMF, we should also signal that the conditions associated with the use of Fund resources are made more appropriate and flexible. Unless this is done, countries will prefer to build foreign exchange reserves which would be counter-productive in current circumstances.

We should also agree on a fresh allocation of SDRs of around $250 billion. This would provide the developing countries with about $80 billion of usable resources at a time when liquidity is exceptionally tight.

We support the sale of a part of the Fund's gold to support concessional lending to low income countries thorough the Fund's concessional windows.

The multilateral development banks can play an important role in maintaining the flow of resources to developing countries over the next two years. As an immediate step, we must endorse a 200% increase in the capital of the Asian Development Bank which can be approved by its Board of Governors in May.

The World Bank should also expand its lending in the next two to three years in a manner which helps to fill the gap left by the withdrawal of private capital flows. By directing its lending to infrastructure development and recapitalisation of the banks, it would help to support contra-cyclical policy in a manner which stimulates an early resumption of growth in these economies. To perform this role, the Bank's present single borrower limits need to be urgently reviewed. Its debt to capital ratio also needs to be made more liberal.

We must also take concrete steps to revive trade finance which has been badly hit in part, I regret to say, because of financial protectionism. Export credit agencies can expand their lending. The IFC pool to support trade finance can be substantially expanded, with bilateral assistance from countries in a position to contribute.

An issue of vital concern to developing countries is the rise of protectionist sentiment in the industrialised world. This phenomenon is not surprising, given the downturn in economic activity and the rise in unemployment. However, it will be a test of leadership whether we can persuade the public that we must not repeat past mistakes. We know that the Great Depression was as deep and prolonged as it was because countries resorted to protectionism which triggered retaliatory protectionist responses, leading to a downward spiral.

Leaders of the developing countries have struggled to overcome the doubts and fears of our public to persuade them of the merits of integrating with the global economy. I believe we had substantial success in this effort, and the open economy has brought prosperity to an ever widening circle, in both developing and industrialised countries. These hard won gains will be destroyed if industrial country markets are not kept open in these difficult times. I must emphasise that this is an area where leadership must come from the industrialised countries. I hope the Summit communiqué will contain firm commitment of our intentions to keep our markets open.

Let me now turn to issues of longer term reform of the global financial system. The crisis we have experienced has drawn attention to some basic flaws in the functioning of the banks and other parts of the financial system which enabled a dangerous build up of risks. This experience shows that it is not enough to rely on light regulation of the financial system, combined with market enforced discipline and enlightened managements using in house risk management techniques. We have to move to stronger regulation and improved supervision if we are to prevent a repeat of the crisis. Valuable work has been done by the working groups set up to chart the broad directions of reform in this area. We should endorse the recommendations emerging from this work and entrust the recently expanded Financial Stability Forum and the expanded Basel Committee on Banking Supervision to prepare detailed proposals which can then be used by national regulators to align our national regulations with the new global standards. I think we all agree on the need to expand the perimeter of regulation to cover the non-banking sector, the need to redefine capital requirements to avoid pro-cyclicality, the need to avoid a build-up of excessive leverage and the need to subject systemically important institutions to supervision by a college of supervisors. We should also endorse sharing information and bringing tax havens and non-cooperating jurisdictions under closer scrutiny.

In addition to improving regulation in our individual countries, we also need to develop an effective early warning system which can spot a build up of risks which would threaten global financial stability. This task must be assigned to the IMF in consultation with the expanded FSF. The IMF is the logical institution to deal with this task but I must add that its capacity to undertake even-handed surveillance needs to be greatly strengthened if it is to perform the task well. This is ultimately connected with the governance and accountability of the institution.

The world has changed greatly since the multilateral institutions were established and the role of these institutions needs to be redefined and their mandate suitably revised. The representation of the developing and emerging market countries in the decision making levels of these institutions also needs to be improved. Better representation is essential if the institutions are to have the legitimacy they need to play their role in an increasingly integrated world in which actions taken in one country affect many other countries.

These are longer term issues of institutional reform which we must address once the immediate priorities of crisis management are handled."

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(Release ID :48433)