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Transcript

Challenges for the Global Economy

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George Osborne:

Let me start by thanking DeAnne Julius and the staff here at Chatham House for organizing today's event.

And I am very pleased to welcome to London the new Managing Director of the International Monetary Fund, Christine Lagarde.

I first knew her as a formidable French finance minister, and France's loss is the world's gain as she is already making her presence felt at the Fund.

Christine has taken over at the IMF at a crucial time for the global economy.

We are just eight hours away from the start of the first international meeting of the autumn – later this morning we will travel to the G7 summit in Marseille, to join finance ministers and central bank governors from the world's major economies.

Those meetings need to produce a coordinated plan of action that helps us navigate through the economic turbulence we are all experiencing.

And I think Christine has just set out an extremely clear agenda to achieve precisely that.

As she has just said 'global activity has slowed ... downside risks have increased [and the] global rebalancing of demand growth ... has stalled'.

The challenges we face are more complex than those we faced at the beginning of this crisis, but the underlying cause is the same – excessive levels of debt.

A debt crisis in the banking sector has now turned into a wider crisis of sovereign, banking and private sector debt.

Then we faced a straightforward battle against the forces of deflation and instability.

Now we must contend with competing pressures – market pressures on indebted sovereigns, continued banking instability, a crisis in the Eurozone and continuing imbalances in global demand.

Just as the problems as different, so must be the international response.

And, as Christine has said, each country's response needs to be differentiated.

To repeat the sporting analogy I used on Tuesday – in 2008 the world had to act like a tug of war team, all pulling in the same direction.

Today, we need to be like a football team – with everyone's role suited to their positions and abilities if the team is to be successful.

The agenda for coordinated global action should be clear.

Indeed I agree with Tim Geithner's prognosis that the three most important things are more forceful action in Europe to resolve the debt crisis, getting the US economy moving, and a rebalancing of global demand towards surplus countries.

First, to state the obvious, a debt crisis must be confronted by tackling the debt.

Those countries with large budget deficits and significant fiscal vulnerabilities – including the UK with one of the largest deficits of all – must continue to set out and implement credible deficit reduction plans that will get debt as a percentage of GDP onto a declining path.

As the Managing Director says 'the United Kingdom strong fiscal consolidation is essential to restore debt sustainability, given the UK's very high structural budget deficit and large financial sector relative to GDP'.

That's why our 'policy stance remains appropriate'.

And I agree with her that policymakers must remain alert to risks, and that's why the automatic stabilisers and the ability of monetary policy to respond are key parts of the flexibility built into our plan.

Britain will stick to the deficit plan we've set out.

It's the rock of stability on which our recovery is built.

It's delivered record low interest rates. Abandoning it would put that at risk.

For nothing would be more damaging for Britain at this fragile moment for the world's economy than an increase in mortgage rates for families and an increase in the cost of borrowing for businesses.

It's crucial to remember that simply announcing deficit reduction plans is not enough. They need to be implemented too.

And, of course, in order to be credible, plans must be rooted within credible fiscal frameworks.

In the Eurozone that means member countries should follow the remorseless logic of monetary union and make more progress on institutional reform and fiscal integration.

While, at all times, making sure the UK is not part of it and that our interests are protected and promoted.

The second element of the global response is to accompany credible fiscal consolidation with credible action to strengthen banking systems.

If banking systems are allowed to remain impaired and fragile, then not only will financial instability persist, but the monetary transmission mechanism will remain broken, denying businesses and families the full benefits of low interest rates that are so crucial for recovery.

And here, too, each country's response should be differentiated.

As Tim Geithner, the US Treasury Secretary, said in the Financial Times today 'countries that forced more capital into their banking systems early in the crisis are better placed to support the recovery. Those that did not should move more forcefully now'.

I think the IMF has a huge role to play in making sure this agenda is taken forward, for example with their Financial Sector Assessment Programmes – which are now compulsory for systemic countries.

So dealing with the fundamental causes of this crisis – excessive debt – is critical.

Unless we do that we will simply make the problem worse.

At the same time, however, we need a global rebalancing of demand – the third part of the international response.

We are all familiar by now with what that means.

Current account surplus countries should do more to rebalance their economies and encourage domestic sources of demand.

I spent the whole of yesterday with my Chinese counterpart, Vice Premier Wang Qishan, who explained how China is boosting domestic demand through its 12th Five Year plan.

While this global rebalancing is under way, different countries should take different paths to support demand.

For example, as I said on Tuesday, the US with its reserve currency faces different constraints from other countries, allowing the US the flexibility to take the actions proposed by President Obama yesterday.

For countries with higher deficits, who lack the security of the global reserve currency, and are more exposed to a loss of market confidence, the best way to support demand is to show they can live within their means, helping to keep interest rates low and monetary conditions supportive of growth.

This is precisely what Christine has just explained.

Again, I think the IMF has a central role in this.

With this year's annual Article IV economic assessments of the key economies, they have also produced for the first time what is known as a 'spill-over report'.

This new analysis is exclusive to the countries whose economies have been identified as systemically important – the US, Eurozone, China, Japan and the UK.

They look at the relationship between the individual country's domestic policies and the wider stability of the global economy.

They are an important innovation in macroeconomic surveillance, and complement the other work the Fund has been doing to advise the G20 Finance on how to deliver strong, sustainable and balanced growth.

The final element of the global agenda must be a concerted effort to open up markets and reform our economies to make them more productive.

In particular, at a global level there could be no greater stimulus than renewed progress on global trade talks.

And we urgently need a real push towards improving the functioning and transparency of oil markets, increasing supply and bringing oil prices down from their current elevated level.

This is the right international agenda for the world economy.

I support it.

The IMF has advocated it.

It should form the basis for our international discussions later today.

And for all the international meetings that are to come later this autumn.

The world needs political leadership, and with this agenda we have the chance of delivering just that.

Thank you very much.