Conference on Achieving Financial Stability
- Lessons from the Eurozone Crisis for Macroeconomic and Financial Stability -
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INTRODUCTION

Good morning, everyone. It is a great pleasure for me to welcome you all here today. On behalf of the Japanese Ministry of Finance, I feel very honoured to host this important conference with our colleagues from the ADBI.

As you know, the main objective of this conference is to learn lessons from the European sovereign debt crisis. Although this is still an ongoing crisis, it seems that initial lessons have already been emerging, which have important implications for policymakers and academics around the world. So, I think this conference provides a timely opportunity for us to take stock of these emerging lessons and to prepare ourselves for the next crisis.

In my view, the European debt crisis has three unique characteristics. The first is that the crisis of public finance and the crisis in the financial sector have occurred in a simultaneous manner. The second is that the spillover from the crisis has spread to all over the world, including the Asian region in which we have a strong interest. The third is that the crisis is taking place in the eurozone where the member countries share the single currency and monetary policy, while other policies including fiscal policy remain largely in the hands of each member country.

Based on these observations, I would now like to talk about three things. One is about the Japanese public finance, and the second is about regional safety net in Asia, and finally I will touch on the role of the IMF in addressing the European debt crisis.

Japanese Public Finance

So, let's start with the Japanese public finance.

Obviously, one of the most important lessons from the European debt crisis is that the deterioration of fiscal situation could have a very negative impact on the financial sector, as well as on the economic growth.

Actually, the Japanese fiscal situation is much worse than that of Greece. In 2011, the Japanese fiscal deficit is as large as 10% of GDP and its debt to GDP ratio has risen to 230%. Also, about 70% of the Japanese government bonds are held by the domestic private financial institutions. Of course, having a stable domestic investor base is an advantage from debt management perspective. But at the same time, this close link between the sovereign debts and the financial institutions could also imply that the Japanese financial system is more vulnerable to fiscal shocks than in Europe.

With regard to the fiscal policy, Prime Minister Noda has been reiterating that the situation in Europe is not "the fire on the other side of the river", and is determined to press ahead with fiscal consolidation measures. Indeed, the government decided on the comprehensive plan for social security and tax reforms last month, which includes a rise in the consumption tax rate. The government is preparing to submit the necessary bills to the Diet by the end of this month.

Regional Financial Cooperation in Asia

Next, I will turn to the regional financial cooperation in Asia.

Despite the uncertainly surrounding the international financial markets, the Asian region has been maintaining sound economic growth. And thanks to sound economic policy after the Asian financial crisis in the late 1990s, the resilience of the region against external shocks has increased. Having said that, I don't think we can be complacent, as there are recent signs that the deleveraging by the European financial institutions has been affecting the region. To prevent contagion from the European debt crisis, it is important that Japan take the lead in strengthening the regional financial safety net in Asia.

With our colleagues from ASEAN+3 members, we are now working hard to strengthen the CMIM. Specifically, we are considering increasing the size of the CMIM from current 120 billion U.S. dollar. Also on the table is introduction of the crisis prevention function to the current CMIM.

In addition to these efforts at regional level, we are also strengthening safety net at bilateral level. I'm not going into details here, but let me just mention that late last year we agreed on the enlargement of bilateral swap agreements with Korea and India.

Role of the IMF in Addressing the European Debt Crisis

Now, I'll talk about the role of the IMF in addressing the European debt crisis.

It is fair to say that since the European debt crisis has become a global issue, the IMF has a role to play as a global institution. But when it comes to the question of what kind of role the IMF should play, the answer is not so easy. In my view, the challenges which the IMF is currently facing are unprecedented for the following three reasons.

First, in the past the IMF's financial assistance has been targeted mostly to emerging and developing countries. Before the European crisis erupted, the IMF had not assisted highly developed area like the eurozone with large capital flows and financing needs. Let me show you statistics to illustrate this point. During the Asian financial crisis in the late 1990s, the scale of IMF's assistance to countries like Korea, Thailand and Indonesia was around 3% to 5% of each recipient country's GDP. But the scale of the IMF's assistance to Greece, Ireland and Portugal during the current crisis is around 13% to 14% of each country's GDP.

The second point is about the denomination of liabilities. In the Asian and Latin American financial crisis in the past, the cause of the crisis was debts denominated in foreign currency, namely, the U.S. dollar. So, there was a strong case for external help. On the other hand, in the current European crisis, the cause of the problem is debts denominated in domestic currency (euro), and the eurozone has its own central bank (ECB), which can theoretically issue unlimited amount of the domestic currency needed to solve the crisis.

Third, the GDP of the eurozone countries such as Italy and Spain is far larger than that of IMF programme countries in the past.

Given these factors, we believe that the role of the IMF in addressing the European debt crisis should be limited to complementing the European self-efforts, and the IMF cannot substitute for the European firewall. Although the Japanese government is prepared to consider expanding the IMF resources and making bilateral contribution to it, we believe further efforts by the Europeans themselves are necessary beforehand.

At the G20 ministers' meeting in Mexico City last month, we reached an agreement that the European reassessment of its own firewall in March will provide an essential input in considering additional resources to the IMF. I believe this is a very sensible agreement, totally in line with the position of the Japanese government. As you know, Europe is due to reassess the adequacy of the scale of EFSF and ESM by the end of this month, and we are anxiously waiting for the outcome.

CLOSING

To conclude my speech, I think the European debt crisis poses very fundamental issues such as the nature of currency, the responsibility and limitation of states, and the role of global institutions like the IMF. I hope this conference will offer a very productive and fruitful discussion, and help us understand these core issues more deeply.

I will stop here. Thank you very much for your attention.