Address by Murilo Portugal
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Mr. President, Excellencies, Ladies and Gentlemen,

It is a great pleasure to address this distinguished audience again and to share with you the IMF's views on current economic developments and the outlook for the global economy.

The global economy is slowing in the wake of financial dislocations and the effects of soaring commodity prices on global demand. However, global activity seems to be more resilient to the financial shock than the IMF originally feared. At the ECOSOC meeting last April, the IMF was projecting that global growth would slow to below 4 percent in 2008 and 2009, following 4.9 percent growth in 2007. However, actual growth in the first quarter of 2008 has been stronger than anticipated. As a result, our growth forecasts for 2008 are likely to be revised up a notch. But we still anticipate a protracted slowdown. The outlook for global growth for 2009 will likely remain broadly unchanged from our April forecasts.

Growth in the United States fell below one percent in each of the last two quarters, reflecting continuing distress in the housing and financial sectors and slowing private consumption. The downturn appears likely to be more drawn-out than usual. In the **Euro area**, growth is likely to slow, following a first quarter stronger than we anticipated. **Japan's** GDP also grew faster than anticipated in the first quarter, but domestic demand is likely to weaken, because of higher food and fuel prices and slower wage growth. **In emerging and developing economies,** growth is projected to moderate only modestly in 2008 and 2009. This reflects robust domestic demand and the strong growth of export receipts in some commodity exporters.

But there are important downside risks to this outlook:

- **First, inflation risks, rooted largely in rising commodity prices, have accelerated,** limiting central banks' room for maneuver in support of growth. Central banks in some countries have already begun tightening policies to head off second-round effects of the recent price hikes on core inflation, and to re-anchor inflation expectations. Inflation risks are a particular concern in some emerging economies, where monetary policy makers face constraints from inflexible exchange rate regimes.

- **Second, while financial sector risks have moderated and markets begun to stabilize, overall market confidence remains fragile.** Central banks have demonstrated their commitment to forestall systemic events, and financial firms have made progress in recognizing losses and replenishing capital. Yet bank balance sheets are still under strain from accumulated financial losses, despite banks' efforts to raise new capital. Also, the securitization markets remain severely impaired. As economies slow down, the potential for a wider credit deterioration beyond the subprime mortgage market could trigger another round of tightening credit conditions.

- **A third risk is the shifting pattern of global imbalances, which is raising new concerns.** The risks of near-term disorderly adjustment of current account imbalances appear to have eased. However, while the U.S. dollar has declined significantly in real effective terms, this adjustment has fallen disproportionately on currencies of economies with flexible exchange rate regimes. These disproportionate adjustments may be producing new misalignments. Investments of the rapidly expanding surpluses of oil exporters, including through sovereign wealth funds, have raised concerns about some protectionist backlash. Moreover, the increase in capital inflows into some emerging economies could portend growing financial vulnerabilities down the road.

The task of responding to a cyclical slowdown and dealing with financial strains has been considerably complicated by the volatile behavior of oil and other key commodity prices. The recent interest rate cuts in the United States will at some stage need to be unwound, but premature tightening could exacerbate financial strains. In most emerging economies, responding to rising inflation is the most immediate concern. Fiscal policy could play an important complementary role to monetary policy, to help contain rising inflation and commodity price risks. Policy makers would need to respond flexibly to a reemergence of financial strains, and work to rebuild confidence and resilience in the financial system.

Excellencies, Ladies and Gentlemen: the world is facing today a confluence of several challenges. Each of these challenges is serious in its own right, but their combined impact has implications that go beyond managing overall inflation or financing higher import bills.

Higher food and fuel prices confront many developing countries with serious questions about the right macroeconomic response. Among these questions:

- How are the price increases affecting the prospects for achieving the MDGs? What policies can be used to protect hard-won gains in poverty reduction in a sustainable and financially viable manner?

- Can countries mobilize additional financing to pay for immediate measures and higher import bills without diverting resources away from other uses critical to the MDGs?

- What is the right balance between short-term financing and adjustment in the responses to the increased prices? What are the best instruments for this adjustment?

Making the right choice on these questions is further complicated by other challenges that are being brought into stark relief by the rise in food, energy and commodity prices. Higher fossil fuel prices reinforce the attractiveness of biofuels as an alternative energy source. But we must ensure that arable land is not taken out of food production and assigned to biofuels production. Moreover, biofuels production should be driven by market forces, and not by distortionary support subsidies in individual countries.

In an increasingly globalized economy, where world supply for highly traded products falls short of demand and supply cannot be quickly increased, prices will rise—sometimes dramatically as we have seen. While some countries—especially net food and oil importers—are being more affected than others, prices have risen for all and no one country will be immune from their impact on global growth. No one country can overcome all the complex and interrelated challenges on its own. International cooperation and institutions are needed to help find global solutions to interrelated global problems. International institutions should not operate in isolation or compartmentalize the work needed on food prices, on climate change, on biofuels and on achieving the millennium development goals. Our efforts must be coordinated to successfully meet the challenges.

We are seeing good examples of how this coordination can be achieved. Within the UN system, the Secretary General's High-Level Task Force on the Global Food Price Crisis, and the MDG Africa Steering Group have brought together different actors, each with its own area of expertise and comparative advantage, but each firmly committed to finding consistent solutions to the issues at hand. Such joint work is more important than ever before. I can assure you that the IMF remains committed to play its part to help find solutions to these global issues.

Thank you for your attention.