U.S. DEPARTMENT OF THE TREASURY

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Testimony of Treasury Under Secretary for International Affairs Nathan Sheets before the House Financial Services Subcommittee on Monetary Policy And Trade

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WASHINGTON - Chairman Huizenga, Ranking Member Moore, and Members of the Committee, thank you for the opportunity to testify today. I appreciate the opportunity to discuss Treasury's role in promoting global economic growth.

Earlier this month, I joined Secretary Lew at the G-20 Finance Ministers and Central Bank Governors meeting in Ankara, Turkey. Discussions at the meeting focused on the recent turbulence in global financial markets, and in China in particular, as volatility in its equity and currency markets has spilled over to markets globally. Fears of a slowdown in China have also raised concerns about the regional and global growth outlook. Commodity producers have been especially vulnerable to lower Chinese demand. We discussed ways to boost global demand, including through fiscal policy, strategic infrastructure investment and structural reforms, as well as the need to continue to strengthen financial supervisory and regulatory practices to reduce the risk of financial crisis.

In Ankara and elsewhere there has been a great deal of interest in recent developments in China. The Chinese economy is undergoing a difficult but essential transition that, if successful, will make growth more reliant on domestic consumption and less on exports and investment. The Chinese government has laid out a comprehensive set of economic reforms to move toward a more market-oriented, consumer-driven economy. These reforms are largely consistent with what the United States has long advocated. To ensure that the transition is managed in an orderly way, China must transparently communicate its policies and actions and allow the market to play a primary role in determining outcomes. Treasury has had sustained and robust engagement with China on its policies – including in the economic track of the U.S.-China Strategic and Economic Dialogue – and in light of recent developments we are pushing the Chinese to accelerate the implementation of its reform agenda, while underlining that to bolster their effectiveness these reforms must also be implemented in a transparent manner.

Turning back to the global arena, our partners look to U.S. leadership to help formulate the international agenda. And we, in turn, rely on the international financial institutions (IFIs) to provide analytical, technical and financial support to identify vulnerabilities, advance reforms, and smooth adjustment. In the aftermath of World War II, the United States drove the creation of new institutions – the International Monetary Fund (IMF) and the World Bank – to reduce economic conflicts, avoid beggar-thy-neighbor policies, provide support for countries in crisis or transition, advance pro-growth economic reforms and promote growth in low-income economies. Over the years, we have also played a leading role in the regional development banks in Latin America, Asia, Africa, and Europe. The partnership between the United States and these institutions has continued with the support of multiple Administrations led by Presidents of both parties, because these institutions have proven their worth. They are vital to our economic interests, and our investment in these institutions means that we are able to shape their policies to maximize U.S. and global prosperity.

By that measure, we have been quite successful. Since 1950, U.S. GDP has risen more than 7-fold and global GDP has risen more than 10-fold, while global poverty has fallen dramatically. Over this period, the improvement in economic performance and the reduction in poverty have been most pronounced in emerging market and developing economies. Stability and increased prosperity in other parts of the world not only provides growing markets for U.S. products and increasing investment opportunities for Americans, but also strengthens our security by reducing civil unrest and regional conflicts.

The IMF has played and continues to play an important role in providing assistance to key strategic partners of the United States. For example, in Ukraine, the IMF is currently supporting a program that aims to bolster the Ukrainian government's extraordinary reform efforts. Notwithstanding Russia's aggression, the authorities have taken difficult steps to improve fiscal discipline, decrease distortionary energy subsidies, improve social assistance for the most vulnerable, tackle corruption, reform state-owned enterprises, and initiate financial sector repair. This example highlights the importance of the Fund in addressing challenges that are at the core of America's interests abroad. Further, IMF financial assistance for Ukraine has been crucial for catalyzing additional support from other bilateral and multilateral partners.

In recent years, the IMF has been critical in helping Europe avoid an economic meltdown, even as the Europeans provided the lion's share of the financial assistance and bore the brunt of the financial risks. Europe's economic woes, especially in the 2010-2012 period, could have caused major harm to the United States. Between May and July of 2010, at the very time we were seeking to put the Great Recession behind us, the stock market in the United States declined by about 15 percent, largely on these European developments, wiping out about $2 trillion in capitalization. The IMF's important technical role went far beyond its financial investment, which is currently only about one-tenth that of Europe's. The IMF's programs in Europe are proving effective, as euro-area authorities have developed new tools to fight crises and ensure financial stability and as vulnerabilities in the "peripheral" countries are greatly reduced. Ireland and Portugal have emerged from crisis and are making early repayments to the IMF.

In Greece, the IMF has been a key partner in Europe's efforts to support a difficult but necessary adjustment that encourages growth and puts debt on a more sustainable path. We stand behind the IMF Board's 2010 decision to provide the IMF with limited flexibility in its policy for exceptionally large financing, enabling the Fund to support Greece at a critical time and in a manner that meaningfully reduced the risk of renewed global crisis. In 2012, the United States supported the IMF's judgment that debt reduction was needed, and the United States and the IMF are actively supporting the need for further debt relief for Greece now.

The IMF's crisis response in the Middle East and North Africa (MENA) region has been crucial to encouraging macroeconomic stability in several countries that are significant to our national security. For example, the IMF has supported Jordan with exceptional financing as the country deals with significant economic pressures stemming from refugees and the regional crisis. And in Africa, the Fund, responding to calls by Secretary Lew, was also at the forefront of emergency financial assistance in the form of highly concessional loans and debt relief to Guinea, Liberia, and Sierra Leone to help counteract the scourge of the Ebola virus. Closer to home, and again after calls by the United States, the IMF has been providing support to Haiti as it goes through a difficult period of political and economic reform.

In 2010, building on earlier efforts to reflect the growing importance of major emerging markets in the global economy, the membership of the IMF agreed on a set of quota and governance reforms. These reforms are designed to strengthen the finances of the IMF and give a greater voice to dynamic emerging markets, such as Brazil, China, India and Mexico, while preserving the U.S. veto by a comfortable margin.

As the largest shareholder and the only member with veto power over major IMF decisions, our extended delay in approving the 2010 IMF quota and governance reforms has led our partners to question our commitment to the multilateral system. Some countries have pursued their interests in other ways, including by creating new institutions in which the United States has no voice, such as the New Development Bank (known as the BRICS bank) and the Asian Infrastructure Investment Bank (AIIB).

To ensure that the IMF remains at the center of the multilateral economic system – and that we maintain an important voice in it – the United States should promptly approve the 2010 quota and governance reforms. Our interest in strengthening the Fund is not based on esoteric notions of global leadership or nostalgia for institutions that the United States created. Rather, we have learned from hard-won experience that a well-resourced and effective IMF is indispensable to achieving our economic and national security interests. By stemming crises in other countries and preventing them from spreading around the globe, the IMF protects U.S. jobs and exports. The IMF's policy advice and financial support also foster countries' economic growth, thereby helping boost global demand.

The proposed reforms of the IMF's quota and governance will put the IMF's finances on more stable footing by doubling the size of quotas and reducing the IMF's reliance on borrowed resources through a reduction in the New Arrangements to Borrow (NAB). Quotas are the IMF's core resources that reflect the shares each country holds in the institution. Quota shares are directly related to voting shares and hence the voice of each member in the IMF.

Increasing our quota under the proposed reforms will not raise the current U.S. financial commitment to the IMF. The U.S. quota increase will be matched by an equal reduction in the U.S. financial participation in the NAB. But, the shift to quota resources signifies a stronger commitment to the core resources of the institution and will allow the IMF to reallocate voting shares and modernize its governance structure.

From a financial perspective, our investment in the IMF is exceptionally sound. U.S. claims on the IMF are of the highest quality – they are protected by the IMF's rock-solid balance sheet, with substantial reserves and unrealized gold profits that exceed total IMF credit outstanding.

The Treasury Department also fosters growth and prosperity by working in partnership with the multilateral development banks, including the World Bank and the regional development banks. Like the IMF, the MDBs' purposes firmly align with the interests of the United States, and they are vital tools for promoting security, economic growth, environmental sustainability, and poverty reduction. In particular, the MDBs are a cost-effective means for the United States to support critical investments in developing and emerging economies. Our $2.2 billion budget request for the MDBs for FY 2016 supports more than $100 billion in annual MDB assistance for developing countries.

The United States led the establishment of the MDB system and has been a driving force in the evolution of the MDBs over the past 70 years. We work closely with their management and other shareholders to help shape their priorities and get them quickly engaged in countries of strategic importance to the United States. In many cases, we coordinate programming so that the MDBs' extensive on the-ground-presence, diverse financing instruments (including debt, equity, and guarantees), deep data and knowledge capacity, and strong and trusted relationships with national policymakers amplifies our direct bilateral assistance.

To ensure that these institutions keep delivering on our priorities, sustained U.S. engagement will be crucial. Treasury is working to advance a robust reform agenda at the MDBs. We are focused on securing a revised set of safeguards at the World Bank that deliver improved social and environmental outcomes by providing additional protections for vulnerable and disadvantaged groups, adding new provisions on the health and safety of workers, and enhancing the implementation and monitoring of the environmental and social impacts of World Bank projects. We have supported updates to the World Bank's procurement policies that will benefit both U.S. businesses and the poor in developing countries. The MDBs must also continue to build the capacity of their independent evaluation units to increase accountability and maximize development impact.

We must also pay attention to the MDBs financial capacity to deliver on key investments needed for countries to progress on their path to sustainable development. We are exploring options for the MDBs to optimize their balance sheets, so as to expand their lending capacity while relying on existing resources. We are calling on emerging donors, including China, to contribute more to the MDBs' concessional windows, in recognition of these countries' increasing importance in the global economy. And we are urging management and staff from the MDBs to work to help countries mobilize their own domestic resources and private sector finance to support their development.

This is an important moment for the United States at the MDBs, as some countries are seeking to weaken these institutions' high standards and correspondingly questioning our leadership role. Sustaining our leadership, influence, and credibility, and maintaining our shareholding, requires fully funding our current and past commitments to the MDBs' non-concessional and concessional windows. Let me describe, through a few illustrations, the ways in which our commitments to the MDBs are vital to advancing U.S. priorities.

The MDBs complement and amplify our bilateral development assistance. The IDB is helping Central American countries implement economic and social reforms to address many of the root causes and effects of violence and migration, working closely with the World Bank and USAID. The African Development Bank (AfDB) and World Bank have pledged over $8 billion in support of the President's Power Africa Initiative, which aims to extend electricity access to over 60 million households and businesses.

The MDBs' work helps us combat threats to national security. The World Bank and European Bank for Reconstruction and Development (EBRD) provided more than $5 billion in 2014 to Ukraine for economic stabilization and energy security, and cut off new assistance for Russia. They are on track to provide a similar level of funding this year. The World Bank, AfDB, and EBRD are supporting small entrepreneurs and promoting reforms to the business climate that help create jobs in North Africa and the Middle East, reducing the lure of extremism.

The MDBs' significant investments in infrastructure facilitate the movement of people and goods and support investment, for example by reducing costly electricity cuts that stymie production. In this way, the MDBs help developing countries contribute to global growth and build new export markets for the United States. In just one example, the Asian Development Bank (AsDB) is helping to integrate markets in Southeast Asia by financing regional roads and in Central and South Asia by financing new energy connections.

The MDBs are also critical partners in preventing and responding to global crises and disasters, such as the Ebola outbreak, or the 2010 Haiti earthquake and the more recent Nepal earthquake.

Finally, the Administration's trade agenda is also essential to our efforts to promote prosperity. We are working to secure a final Trans-Pacific Partnership agreement (TPP) that unlocks export markets, establishes strong rules, and fosters stronger economic growth at home. TPP promises to help U.S. businesses reach customers in the world's fastest growing region, deliver more and better jobs in the United States, and elevate standards for trade and investment throughout the TPP region, including with regard to promoting transparency, fairness, innovation, labor rights, and the environment. By promoting important market-oriented reforms, we expect TPP to contribute to stronger and more balanced economic growth in our partner countries and to encourage closer economic integration. In addition, we are making progress with the European Union on the Transatlantic Trade and Investment Partnership (T-TIP) to expand what is already the largest trading relationship in the world. We are also negotiating a bilateral investment treaty with China to open up China's highly restrictive system to foreign investment and help create a wide range of opportunities for U.S. firms to participate in the Chinese market. Finally, negotiation of the Trade in Services Agreement with more than twenty other partners presents an opportunity to remove impediments to exports across all services sectors and boost U.S. growth and support additional jobs.

As we continue to work with Congress on promoting economic growth both here at home and throughout the world, maintaining our leadership role in the IFIs and moving forward on the Administration's trade agenda are crucial. I look forward to working in collaboration with this Subcommittee to address these critical issues.

Thank you. I am happy to answer your questions.

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