Grim mood in IMF and World Bank

By Alan Beattie and Chris Giles in Washington

There is a grim mood about the meetings of the International Monetary Fund and World Bank, for which ministers gathered on Friday in the gloom of a grey rainy day in Washington.

But the grimness of the determination of eurozone attendees to get a grip on Greece was often matched by gloom from others that they were forced to sit and watch while Europe struggled to organise itself.

Eswar Prasad, former head of the IMF’s China division and now at the Brookings Institution in Washington, said: “The crisis of confidence cannot be stanched merely by broad statements of concern and noble policy intentions at a time when decisive and concerted policy actions are sorely needed”.

Mr Prasad added: “In the absence of specific and decisive policy measures, markets are unlikely to be calmed by such broad statements”.

Unfortunately, that is largely what they got. The G20 grouping of leading economies, which has largely been absent from the management of the crisis so far, did at least rouse itself to issue a statement after it met for dinner on Thursday evening – previously it had planned to slip, communiqué-less, into the night.

But it was with deep irony that one attendee referred to the bland communication as “poetry”. The only linguistic innovation in the statement was that the European financial stability facility, the eurozone’s bail-out fund, would be extended to “maximise its impact”.

This appeared to be the strongest statement that ministers were prepared to make to try to reassure the markets while not scaring European parliamentarians, some of whom have yet to approve an extension of the EFSF’s powers.
There have been proposals – supported by the US and others – to increase the size of the EFSF by using those new powers to leverage its impact by guaranteeing debt. George Osborne, UK chancellor of the exchequer, said: “I’m not sure it is adequate, but that has to be a matter for the eurozone itself ... What is required is a sense from markets that there is enough firepower.”

As it frequently has during the crisis, European constitutional nicety had to take precedence over the imperative to get ahead of the problem. Eurozone ministers, not wanting to alarm those legislatures that have yet to agree to extend the EFSF – including the German Bundestag – have been deliberately vague about how it might be augmented.

François Baroin, the French finance minister, told reporters on Friday it was “very difficult for Americans to understand” how a currency could work with so many parliaments – though added that the US itself seemed to be having enough trouble with just one.

Mr Baroin has dropped the strongest hints of anyone about the EFSF’s future, using the term “leverage” when discussing it. On Friday he said that the EFSF could establish a legal tie with the European Central Bank without having to go through another round of parliamentary approvals – a key step in leveraging the resources of the EFSF by allowing it to issue lending guarantees.

“Maximum impact means using full flexibility ... it has to be clearly linked to the ECB,” he said. Joint efforts by the ECB and the EFSF “are clearly planned for in the agreements”, he said.

In the mean time, developing and emerging market countries have urged the eurozone to deal with its crisis before it provokes a global recession that is likely to drag down poorer economies with it.

“There is a risk that the sovereign debt crisis of some countries becomes another financial crisis,” said Guido Mantega, Brazil’s finance minister, following a meeting with his counterparts from the Bric [Brazil, Russian, India, China] countries. “We eased the 2008 crisis by fast and co-ordinated actions within the G20,” he said. “We need to do the same now.”

But the emerging markets have retreated somewhat from earlier suggestions that they themselves could undertake a big support operation to help the eurozone.

Ministers from the Bric countries have offered to help boost available resources for bailing out banks and sovereigns, with some suggestion that they could add to the fire
power of the EFSF, perhaps by lending alongside it. But eurozone ministers say they have received no concrete proposal on the matter, beyond the uncontroversial contention that emerging markets could buy the triple-A rated bonds issued by the EFSF.

Attendees were already looking forward to the G20 heads of government summit in Cannes in early November as the deadline for the eurozone to get its act together. On the strength of the past 18 months, though, many were looking forward in hope rather than confidence.