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G8 finance ministers see crisis easing

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Finance ministers from the G8 on Saturday signalled their cautious belief that the worst of the global financial crisis might be over and began for the first time to discuss “exit strategies” to counter the growing threat of inflation.

Stress tests for banks were also discussed, aides said, but divisions over the issue – with France and Germany resisting calls for more transparency over publication of results – kept an explicit mention of tests out of the final communique.

“There are signs of stabilisation in our economies, including a recovery of stock markets, a decline in interest rate spreads, improved business and consumer confidence, but the situation remains uncertain and significant risks remain to economic and financial stability,” the communique said after a weekend of talks in the southern Italian city of Lecce.

An official said the reference to “significant risks” – absent in the draft – was inserted at the request of the UK. An earlier mention of “encouraging figures in the manufacturing sector” was deleted from the draft after eurozone industrial production data for April, released on Friday, showed an annual drop of more than 21 per cent.

Ministers also warned that unemployment might continue to increase even after economies start growing again.

For the first time G8 ministers tackled growing market concerns over unsustainable levels of public debt and budget deficits that have weighed on US Treasury bonds and the dollar.

“We discussed the need to prepare appropriate strategies for unwinding the extraordinary policy measures taken to respond to the crisis,” the statement said. “These ‘exit strategies’, which may vary from country to country, are essential to promote a sustainable recovery over the long term.”

The ministers – from Canada, France, Germany, Italy, Japan, Russia, the UK and US – asked the IMF to prepare an exit strategy analysis.

Officials said Germany’s Peer Steinbrück was the most emphatic about the need to address inflationary pressures. Other ministers also raised concerns about mounting commodity prices, particularly oil. Giulio Tremonti, Italy’s finance minister, warned against market speculators.

“Instead of financing the real economy, the extra liquidity in the system has the tendency to fuel speculation,” said Mr Tremonti, a long-standing sceptic of the efficacy of fiscal stimulus packages.

Alastair Darling, UK chancellor, played down talk of exit strategies, telling reporters there had been only brief discussion. “We are not there yet. No one is talking about exiting now. That’s some way down the track,” he said.

Asked if he was more worried about deflation or inflation, he said one always had to be vigilant about inflation, and noted the Bank of England’s 2 per cent target.

Mr Tremonti also urged caution about future recovery prospects despite signs of pick-up. “We are still on terra incognita,” he told a news conference.

Tim Geithner, US Treasury secretary, was also cautious. “I don’t think we’re at the point yet where we can say we have a recovery in place,” he told reporters. But he added that policies adopted had eased concerns about a more severe recession, deflation and systemic risk in financial markets.

In a prepared statement he said it was “too early to shift toward policy restraint” but that economic and financial recovery would be stronger “if we make clear today how we get back to fiscal sustainability when the storm has fully passed”.

However, aides said the atmosphere was considerably more positive than during the G20 summit in London in early April. Ministers believe that some forecasts will start to be revised upwards rather than getting worse.

Eswar Prasad, a Cornell University professor, commented: “There is a distinct shift in tone from concerns about avoiding economic collapse to concerns about how to withdraw fiscal and monetary stimulus and exit from government involvement in financial institutions."

He said it was interesting that France and Germany, facing prospects of very weak recoveries, were the most vocal in cautioning against the risks of stimulus measures while pushing aggressively for broadening financial regulation.

"US, Canada, UK and Japan seem more willing to consider further stimulus if the recovery doesn't pick up steam. These countries are also taking a more guarded approach to financial regulation," commented Mr Prasad.

On an intiative driven by Italy, the meeting agreed to develop what it called the Lecce Framework – "a set of common principles and standards regarding the conduct of international business and finance", which Mr Tremonti has christened a Global Legal Standard.

The standards, to be elaborated by the OECD, focus on five areas: corporate governance, market integrity, financial regulation and supervision, tax co-operation and transparency of macroeconomic policy and data.