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Conference on reform

Involving the private sector and preventing financial crises are main topics for discussion

Because the international monetary and financial system is a "public good," all have an interest in improving it, IMF Managing Director Michel Camdessus said during a conference entitled Key Issues in Reform of the International Monetary and Financial System in Washington, hosted by the IMF's Research Department, on May 28–29. The conference, which was organized by Michael Mussa and Alexander Swoboda, in collaboration with Peter B. Kenen, took a critical look at issues central to the discussion of how to strengthen the system, including coping with capital flows, coordinating exchange rate policies, providing financial assistance to countries facing external payment difficulties, and preventing and resolving financial crises. Participants included academics, senior government officials, members of the press, IMF Executive Directors, and IMF staff. Camdessus and Jacob Frenkel, Governor of the Bank of Israel, delivered keynote addresses, and IMF First Deputy Managing Director Stanley Fischer provided closing remarks.

Alexander Swoboda (left) and Michael Mussa, organizers of the conference, coauthored a paper, with colleagues from the Research Department, on capital flows to emerging markets.

Highlights of the conference are covered on pages 194–200. *(Please turn to the following page)*

Bretton Woods Committee

Stable, integrated world economy will depend on mature relationships, sustained political support

With the Asian crisis receding, the world is beginning to shift gears—absorbing the lessons of a volatile decade and taking up again the task of creating a more stable world economy. The U.S.-based Bretton Woods Committee used its annual meeting on June 9 to assess the daunting challenges facing the Bretton Woods institutions and the world economy as the new millennium approaches. Members of the committee heard from prominent U.S. congressional leaders and Dwayne Andreas of Archer Daniels Midland Company; from the heads of the IMF, the World Bank, and the International Finance Corporation, and from Robert Rubin, outgoing U.S. Secretary of the Treasury, who delivered the keynote address. The meeting also featured a panel discussion on the merits of IMF financing from private markets.

Camdessus: The basis for successful crisis resolution must be laid before crises strike.

IMF Managing Director Michel Camdessus underscored how much the future stability of the world *(Continued on page 206)*

Mitigating instability under high capital mobility

(Continued from front page)

Exchange rates among major currencies

Past attempts to coordinate action among the major currency countries to limit the damage caused by exchange rate instability have met with little success and have even led to questions about the need for such efforts, according to Benoît Coeuré and Jean Pisani-Ferry. However, Pisani-Ferry, who presented the paper, said two recent events have reopened the discussion—the exchange rate crises in emerging economies, which some observers have traced back to the effect of the strong dollar on currencies that were formally or informally pegged to it, and the creation of the euro and its possible impact on the international monetary system.

Jean Pisani-Ferry (left) and Benoît Coeuré called for a new approach to policy coordination.

Exchange rate coordination in the post–Bretton Woods era has been a process of trial and error, Pisani-Ferry said. Attempts have ranged from highly ambitious schemes with internationally agreed targets, such as the Plaza and Louvre accords of 1985 and 1987, to more modest schemes, with ad hoc interventions in the case of extreme misalignments only. Neither approach to coordination was able to secure lasting stability.

Coordination may be more feasible now than in the 1980s, Pisani-Ferry said, because the situation is different and countries are more knowledgeable about the results of misalignments and lack of coordination.

A renewed international arrangement should dissociate the two objectives that target zone schemes closely associate: policy coordination and exchange rate stabilization. There is still a case for monitoring exchange market developments, but not for targeting specific values of nominal exchange rates. Pisani-Ferry and Coeuré proposed a two-pronged approach: a coordinated response to macroeconomic shocks accompanied by a monitoring of foreign exchange developments. The steps they recommend for implementing this arrangement are

- the joint endorsement by the United States, Japan, and Europe of a core set of broad macroeconomic policy principles.
- development of commonly agreed principles for deciding on the fiscal and monetary response of each participant to shocks.

Pisani-Ferry and Coeuré also suggested that estimates of equilibrium exchange rates could be used to structure Group of Seven discussions on exchange rate developments and provide some guidance for market assessment. The IMF could be asked to produce and release such estimates on a regular basis, as part of its surveillance exercise.

Discussion. Most discussants agreed with Pisani-Ferry and Coeuré that excessive exchange rate volatility could be destabilizing and disruptive. They also agreed with many of the authors' suggestions for policy coordination (except for the suggestion that the IMF produce and release equilibrium exchange rates), although most were skeptical about their practical application.

Alan Blinder wondered if any of the proposed strategies would reduce short-term volatility. Also, domestic policies in the major countries are not always consistent; and the exchange rate—rather than the interest rate—should be allowed to absorb some of the effects of an external shock, he added.

Horst Siebert noted that a multilateral approach to stabilizing exchange rates requires countries to adhere to stability-guaranteeing rules that all relevant policies in the three major regions would be harmonized, thereby relinquishing sovereignty over monetary policy. This is not realistic and may not be desirable.

Ricardo Hausmann said he saw a trend toward fewer currencies, which would make it easier for countries to hedge their currency risk in euros or U.S. dollars. Ronald I. McKinnon argued that the market's obdurate expectation of trend yen appreciation was a main source of problems for the Japanese and, hence, the world economy. He offered a strategy for dealing with the problem.

Capital flows to emerging markets

The emerging market crises of the 1990s—and in particular the Asian crisis with its global repercussions—have generated perceptions of serious inadequacies in the international financial system and intense debate on global financial reform, particularly regarding capital flows to emerging markets. The aim of the paper by Michael Mussa, Alexander Swoboda, Jeromin Zettelmeyer, and Olivier Jeanne was to focus on the role of international public intervention in forestalling and mitigating future crises, Mussa said.

National policy failures—especially in banking and financial supervision—and a lack of transparency, as well as adverse shocks, helped pave the way for the international financial crises of the 1990s. But there is little doubt, Mussa said, that systemic fragilities also played an important role. In particular, the vulnerability of several emerging market economies to potential financial crises was increased by a sharp progression in the level of their short-term, foreign-currency-denominated liabilities from the 1980s to the 1990s,

Key Issues in Reform of the Monetary and Financial System

Opening remarks
Alexander Swoboda, Senior Policy Advisor and Resident Scholar, IMF Research Department

Keynote addresses
Michel Camdessus, IMF Managing Director
Jacob A. Frenkel, Governor, Bank of Israel

Session I: The Exchange Rate Regime Among Major Currencies
Chairman: Fred Bergsten, Director, Institute for International Economics
Paper:
Benoît Coeuré, Head, Exchange Market and Economic Policy Division, French Ministry of Economy, Finance, and Industry
Jean Pisani-Ferry, Senior Economic Advisor, French Ministry of Economy, Finance, and Industry
Panel
Alan Blinder, Professor of Economics, Princeton University
Ricardo Hausmann, Chief Economist, Inter-American Development Bank
Ronald I. McKinnon, Professor, Stanford University
Horst Siebert, President, Kiel Institute

due in part to an increase in the overall level of debt but also to a shortening of its maturity.

Reform of the international financial system, Mussa noted, has three key objectives: fostering efficiency and growth by allocating capital to where it can generate the highest returns; reducing the risk of international financial crises; and mitigating the impact, and equitably sharing the burden, of crises when they do hit. However, because of asymmetric information and other distortions that prevent any financial system from operating with absolute efficiency, simultaneous pursuit of these objectives gives rise to fundamental tensions. There is no universally applicable, first-best approach for dealing with these problems, Mussa said, and there are inevitably trade-offs.

- While policies that maintain a relatively closed capital account may provide significant protection against international financial crises, they substantially impair a country's ability to take advantage of the efficiency gains from broader participation in the global financial system. More needs to be done to contain the risks and damage of financial crises.
- Efforts to divert capital flows, particularly of short-term credit denominated in foreign currency, into forms that pose less danger of systemic risks run counter to the incentives of economic agents on both sides of the bargain. But it is difficult to establish a sharp dividing line for what constitutes too much short-term debt or to say how far it is prudent to go in shortening maturities and taking on foreign currency debt in attempting to avert a crisis. When a country experiences difficulty maintaining external financing flows, shortening maturities and increasing foreign-currency-denominated borrowings can be quite useful in forestalling a financial crisis. Sometimes, Mussa said, this strategy works, but sometimes it fails, and the subsequent crisis and its costs are enlarged.
- Proposals for bailing in the private sector in financial crises, by requiring private creditors under certain conditions to retain or expand their exposures to a country experiencing an actual or potential financial crisis, also entail trade-offs. The application of such mechanisms for one country in, or on the verge of, a crisis might help that country, but would also be a clear signal for creditors to flee from whatever country they believe might be next on the list for trouble, Mussa said.

The historical pattern of boom-and-bust cycles in international capital flows to emerging markets seems likely to persist, Mussa said. As a result, the time will come again when a number of emerging market countries will face severe external financing difficulties. The reforms to the international monetary system now under way or in prospect should help lessen these problems, but will not make them disappear. Accordingly, there will continue to be a need for official assistance—in appropriate circumstances—with as little subsidy as possible, and subject to relevant conditions, to help countries manage their external payments difficulties and especially to help contain the severe economic damage typically associated with situations of national default. Concern about moral hazard is mitigated, to an important degree, by the conditionality associated with international support packages and by broader international efforts to promote improved national policies.

Discussion. Most discussants thought that sound macroeconomic policy was as key as strengthening the international system. David Folkerts-Landau criticized the paper for attaching too much importance to systemic weaknesses. Rather, he said, financial linkages across emerging markets and fundamental failures in policy in the emerging market economies were the real culprit, not the international financial system. Roberto Zahler observed that the extent to which a country is integrated into the international economy is usually linked to the confidence the rest of the world has in the prospects and management of that economy. This creates a dilemma: sound policies attract excessive capital inflows that threaten the soundness of the economy; as a consequence, measures must be taken—including, in some cases, Chilean-type controls—to manage these inflows.

Michael Mussa (left) confers with Peter B. Kenen, who helped organize the conference and also served on the panel examining the balance between adjustment and financing.

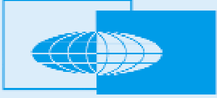
Oldrich Dedek noted that the Czech monetary authorities had found no "silver bullet" for reducing internal and external imbalances and for coping with the ebb and tide of capital flows. The country is seeking entry into the European Union, which requires policy convergence, including of the exchange rate. Eventual participation in the European Economic and Monetary Union would, he said, relieve members of having to use the exchange rate as an adjustment tool.

Rudiger Dornbusch said the emerging market crises might have been averted if the growing stock of debt had been restructured earlier, rather than after the crash. The best way to avoid currency crises, he said, was to "outsource monetary policy," as in a currency board arrangement.

Carmen Reinhart (left) and Guillermo Calvo presented a paper on dealing with "sudden stops" in capital flows.

Balance between adjustment and financing

Developed and emerging market economies share many common symptoms of a financial crisis: large capital inflows, asset price and credit booms, currency overvaluation, and large current account deficits. But as Guillermo Calvo and Carmen Reinhart noted, industrial



Session II: Moderating Fluctuations in Capital Flows to Emerging Market Economies
Chairman: Ernest Stern, Managing Director, J.P. Morgan
Paper
Michael Mussa, Economic Counsellor and Director, IMF Research Department
Alexander Swoboda
Jeromin Zettelmeyer, Economist, IMF Research Department
Olivier Jeanne, Economist, IMF Research Department
Panel:
Oldrich Dedek, Vice Governor, Bank Board, Czech National Bank
Rudiger Dornbusch, Professor, Massachusetts Institute of Technology
David Folkerts-Landau, Chief Economist and Managing Director, Deutsche Bank
Robert Zahler, President, Zahler and Company

Session III: The Balance Between Adjustment and Financing
Chairman: J.J. Polak, former Economic Counsellor, IMF
Paper
Guillermo Calvo, Professor of Economics, University of Maryland
Carmen Reinhart, Associate Professor, University of Maryland
Panel
Montek Singh Ahluwalia, Distinguished Visitor, Stanford University
Yoon-Je Cho, Professor, Sogang University, Korea
Jeffrey Frankel, New Century Chair, The Brookings Institution
Peter B. Kenen, Professor of Economics and International Finance, Princeton University

and emerging market economies part company in the developments that usually follow a speculative attack. Unlike their more developed counterparts, emerging market economies routinely lose their access to international capital markets. Furthermore, Reinhart noted, given the common reliance on short-term debt financing, the public and private sectors in these countries are often asked to repay their existing debts on short notice. These large negative swings in capital inflows—or "sudden stops"—are dangerous. The slowdown or reversal could push the country into insolvency or drastically lower the productivity of its existing capital stock.

New answers to old questions

Following is a summary of remarks by Jacob Frenkel, Governor of the Bank of Israel, during the conference.

Policymaking is being carried out in a new globalized environment that requires new answers to old questions, such as how to conduct exchange rate policy and how to manage capital market flows, Frenkel said.

When capital markets were less open, Frenkel said, the authorities decided when to intervene, where to set the rate, and which regime to follow. Markets and the authorities were in an adversarial relationship. Now, we want to work with the markets, recognizing that market discipline helps to ensure good policies. It is no longer a case of "you versus us," but rather a partnership based on transparency and accountability.

Over the next 10 years, Frenkel said, the trend in exchange rate regimes will probably be toward very fixed or very flexible. In-between regimes will disappear. Countries in intermediate stages should therefore make it clear to the markets that they are in a transitional stage; otherwise, temporary stratagems could be taken as permanent. It was a good idea, he said, to have an exit strategy.

Before making the final jump, countries should make sure they have a parachute, Frenkel said. The exchange rate regime is an important issue, but developing the corresponding markets is essential whatever regime is chosen. Preconditions, such as a functioning exchange rate market and early private sector participation, need to be in place as a condition for fully opening the capital account.

Jacob Frenkel

Making their economy attractive to investors in the economic "Miss Universe contest" is the best way for emerging market economies to regain access to capital markets, Frenkel said. Restrictions on capital flows, even in the interests of controlling sudden reversals in market sentiment, will not attract investors. But evidence of a strong economy and credible policy will bring investors back—even those that had bailed out in recent crises. Markets reward good policy, and countries that adopt the right policies will make the markets quickly forget bad memories, Frenkel concluded.

By the time the crisis erupts and a country has lost its access to international capital markets, the range of policy options available to manage the situation has been severely restricted. The evidence suggests that capital controls do appear to influence the composition of flows, diverting them away from short maturities. However, such policies are not likely to be a long-run solution, and this option has little appeal for countries not wishing to reverse the process of financial liberalization.

Many emerging markets may nevertheless rely increasingly on controls because of a fear of floating and because they lack the discipline that underlies fixed exchange rates. Even when fear of floating does not lead to capital controls, floating exchange rates may have significant costs in terms of both the interest rate volatility associated with them and their procyclical nature.

No serious economist will prescribe the same exchange rate regime for every country, Calvo said. But Latin America already lives in a "semi-fixed world," where the U.S. interest rate has been a crucial variable for national policy since the 1970s. The question is, should these countries stay where they are or go all the way? Strong pegs, like dollarization, can help reduce the incidence of external shocks and may be an attractive option for emerging markets in dealing with the problem of recurring sudden stops. Although full dollarization will not eliminate banking problems, it could lessen them if it reduces the problems stemming from currency and maturity mismatches—and it will do away with speculative attacks on the currency.

Discussion. Most discussants agreed that the time for policy response is immediately after a shock but before the crisis hits. Some objected to the "short shrift" Calvo and Reinhart gave to floating. Montek Singh Ahluwalia suggested that the authors might have focused more on other preventive measures, such as banking sector reform. Yoon-Je Cho noted that when the IMF financing package for Korea was put together, no one had expected that the degree of correction would be so high, and the insufficient financing led to massive depreciation.

Jeffrey Frankel agreed with the authors that the crucial period when the adjustment/financing framework is relevant is right before the crisis. The IMF's recently established Contingent Credit Lines, which could help an otherwise healthy economy defend its exchange rate from speculative pressure, were thus a step in the right direction. Peter Kenen added that steps were needed to limit bank exposure to short-term debt in countries with underdeveloped structures and institutions. Private sector involvement has to be included if the balance between adjustment and financing is to be improved, he said.

Involving the private sector in crisis prevention and resolution

Progress in compelling investors to share the financial burden of a crisis has been slight, Barry Eichengreen

noted. Some analysts have questioned whether moral hazard is a sufficiently overwhelming problem to justify actions that may disrupt the operation of the markets and make it more costly for reputable debtors to borrow. Others assert that a solution to the moral hazard issue may not be possible and that financial and policy innovations can have unintended consequences, including precipitating the very crises they are meant to forestall. Nevertheless, finding ways to ensure that private sector creditors bear their share of the burden is a key step in learning to deal with modern financial crises, Eichengreen said.

The IMF has experimented with a variety of methods for involving the private sector, Eichengreen said, including direct pressure on international banks to lengthen their credit lines in Korea, informal pressure for them to maintain credit lines in Brazil, and asking the government of Ukraine to renegotiate its bonds as a precondition for the extension of official assistance. But the success of each of these approaches depended on characteristics specific to the countries involved.

The IMF and the international community have been trying to find ways of bailing in the private sector, according to Eichengreen, including by adopting new provisions in loan contracts to facilitate orderly restructurings, such as collective action clauses in bonds and creating workable alternatives to ever-bigger IMF bailouts. The addition of such clauses to bond contracts, Eichengreen said, is the only practical way of creating an environment conducive to flexible restructuring negotiations.

Efforts to bail in the private sector will have to proceed on a case-by-case rather than a rules basis, Eichengreen concluded. This approach may seem arbitrary and unwieldy, but at least it does not pose a danger of aggravating the crisis problem as would rules specifying the modalities and circumstances in which creditors would be bailed in.

Discussion. Most discussants agreed with Eichengreen that the private sector had to be bailed in on a case-by-case basis. There is a need to restore capital flows to emerging market economies, especially loans and bond credits, and changes in financial architecture should nourish this return, William Cline said. The objective should be to increase, not reduce, flows. Pablo Guidotti thought that proper management of debt, notably lengthening its maturity structure, was key to reducing public sector financing needs and avoiding excessive recourse to international financial assistance—one of the purposes of "involving the private sector." Innovations in bond contracts are welcome, Guidotti said, if introduced by the private sector to make resolution of future crises more efficient; but IMF policy should not be linked to their introduction.

Barry Eichengreen explored the possibility of making the private sector share more of the burden of financial crises.

J.A.H. de Beaufort Wijnholds said the industrial countries should lead the way in bond rescheduling. The IMF should act as a facilitator to ensure that agreements with the private sector are being observed. Voicing a somewhat contrary opinion, Martin Wolf of the *Financial Times* suggested that since there are such huge difficulties in handling sovereign foreign currency indebtedness, there should be much less of it. Sovereigns should either balance their budgets or borrow in domestic credit markets.

Role of the IMF

Financial role

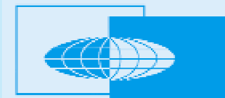
During the emerging market crisis, the IMF was asked to take on exceptional responsibilities under uncertain conditions, David Lipton said. Some observers have been harshly critical of the IMF's performance, while others believe the IMF played a crucial role in helping the world through a difficult and dangerous episode. Maintaining the IMF's readiness to function in the future may require a refocusing of its role, ensuring that it is assigned appropriate tasks and that its legitimacy and public acceptability are reinforced, lest its effectiveness be impaired.

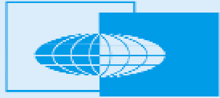
Lipton offered proposals that might help redraw the limits on the use of IMF financial resources by shifting more of the burden of dealing with economic problems to the markets and private sector participants. To start with, he said, the international community should end large-scale IMF financial assistance for member countries with balance of payments problems.

The crises of 1997 and 1998 were unexpectedly severe and filled with uncertainties about capital flows and contagion and the IMF's response was key to preserving the system. But the large financing packages provided only a short-term expedient. It is unreasonable to ask the IMF to continue playing this role, nor is it ideal to assume that these resources will always be available. Lipton said that there is a need to "put the genie of large IMF lending operations back into the bottle" and to restore a more rigid adherence to the use of access limits in approving members' use of its resources.

Among the changes Lipton suggested is a more widespread reliance on flexible exchange rates. The implicit guarantee of a pegged regime in times of stress puts all the onus on the central bank, whereas a floating rate diffuses the stress through the marketplace, he observed.

David Lipton suggested that the burden of dealing with economic problems should be shifted from the IMF to the markets.





Although the IMF has access to borrowing arrangements designed to supplement ordinary resources, the recent crisis made it clear that the potential financial requirements to stem a global crisis are very large and that circumstances could arise in which all of the resources presently available to the IMF could be inadequate to stem the spread of crisis. The international community, Lipton said, should be equipped to react forcefully if some constellation of factors again threatens the international financial system.

Lipton proposed setting up a large pool of resources to equip the IMF to respond if the health and integrity of the international financial system were endangered. A "trust fund" established by a select group of large countries could be used as a last line of defense for the international financial system in time of dire threat. The trust fund would not be an IMF facility, but rather a backstop to the international financial system to be operated in the interests of the international community. The fund would lend freely, and at a penalty rate, as called for in the operation of lenders of last resort. Management of the fund should retain "constructive ambiguity" about the circumstances in which it might be activated.

Discussion. Discussants expressed general skepticism about Lipton's proposed trust fund, and several were not as sanguine about the merits of a floating exchange rate. Jack Boorman expressed doubts about the efficacy of limiting access levels to IMF financing. It is not always easy, he said, to determine when a crisis begins to unfold, whether it will be systemic. Limits would either not be believed by the markets or would tie the hands of the IMF, which needs to be free to stimulate markets and the flow of official and private finance.

Kwesi Botchwey asked what guarantees would be in place to ensure activities of the proposed trust fund would be carried out in a principled way. Charles Calomiris agreed, observing that access would inevitably be delayed and politicized. "Ambiguity," he said, "is open to manipulation in the guise of coordination." Yung Chul Park supported the IMF as crisis manager and lender to emerging

Session IV: Involving the Private Sector in Crisis Prevention and Resolution
Chairman: Sylvia Ostry, Distinguished Research Fellow, University of Toronto
Paper
Barry Eichengreen, Professor of Economics and Political Science, University of California, Berkeley
Panel
William Cline, Deputy Managing Director, Institute of International Finance
Pablo Guidotti, Secretary of Finance, Argentina
J.A.H. de Beaufort Wijnholds, Executive Director, IMF
Martin Wolf, Associate Editor and Economics Commentator, *Financial Times*

Session V: The Financial Role of the IMF
Chairman: Arjun Sengupta, Professor, School of International Studies, New Delhi
Paper
David Lipton, Senior Associate, Carnegie Endowment for International Peace
Panel
Jack Boorman, Director, IMF Policy Development and Review Department
Kwesi Botchwey, Director, African Development Group, Harvard Institute for International Development
Charles Calomiris, Professor, Finance and Economics, Columbia University
Yung Chul Park, Professor, Korea University
Tatiana Paramonova, First Deputy Chairman, Central Bank of the Russian Federation

Is international financial and monetary stability a public good?

Following are edited extracts of an address delivered by IMF Managing Director Michel Camdessus at the conference on key issues in reform, hosted by the IMF's Research Department, in Washington on May 28. The full text is available on the IMF's website (www.imf.org).

Let me start with the proposition that the international monetary and financial system may be seen as a global public good. It is essentially the same system for everyone. If it works well, all countries have the opportunity to benefit; if it works badly, all are likely to suffer. Hence, all have an interest in reforms that will improve the system for the global public benefit.

Coordinating exchange rate policies

There is no world money controlled by a world monetary authority that performs the essential functions of medium of exchange, store of value, and unit of account at the global level. Rather, the moneys of the largest industrial countries do double duty as the moneys for their respective countries and as the moneys used by most other countries for conducting their international trade and financial transactions.

Reasonable stability of the domestic price level is increasingly recognized as the most basic objective of monetary policy. From the global perspective, this domestic orientation of monetary policies in the major currency areas is generally desirable. As experience has unfortunately taught, economic and financial instability in the dominant economies of the world is bad for them and for the rest of the world as well. Thus, economic policies that promote domestic economic and financial stability in the largest economic areas of the world are not only desirable—they are essential—for economic stability and prosperity elsewhere.

Recent experience suggests rather pointedly that more attention can be paid to international consequences and specifically to exchange rates in the management of economic policies in the largest economies with beneficial results for these economies as well as for the rest of the world.

Last September and October, in the wake of Russia's default and the near failure of a large hedge fund, a liquidity crisis gripped a wide range of financial markets. Although adverse effects on the U.S. economy were not apparent, the U.S. Federal Reserve, recognizing the danger posed by this crisis, took the lead among major currency area central banks in easing monetary conditions. In this instance, forward-looking monetary policy action in the United States, the euro area, and Japan, which took account of conditions in global financial markets beyond those of immediate domestic concern, clearly helped to forestall important risks of a deeper global economic downturn and, correspondingly, has helped to create the more favorable prospects for global growth we see today.

We must not, of course, overplay our hand. When domestic considerations relevant for monetary policy in the major countries run counter to external considerations, it will often be a mistake, domestically and internationally, to give much weight to external considerations. Moreover, even when exchange rates may seem to have moved too far, it is not always wise to adjust macroeconomic policies even marginally to try to affect exchange rates.

Concerning intervention, we know it is not a very powerful tool for influencing markets, especially when it is not supported by other policies. However, markets do not always get exchange rates right. Under the influence of bandwagon effects, panics, and other anomalies, markets sometimes take exchange rates a considerable distance away from levels consistent with economic fundamentals in circumstances where this is detrimental to global economic performance. The offi-

market countries, but believed it could provide more information and early warnings to policymakers when it identifies a shift in market perceptions. The IMF should promote closer cooperation between central banks in the Group of Seven and in the emerging market countries.

Tatiana Paramonova said that the Russian experience with stabilization attempts had persuaded her that no single exchange rate regime was optimal for all countries at all levels of development. Relatively clean floating or a currency board would be her choice for emerging markets.

IMF advice

The currency crises in Asia have raised questions about the effectiveness and appropriateness of the conditionality the IMF imposed on crisis countries, Takatoshi Ito noted. It has been alleged that IMF-supported programs did not prevent overshooting of currencies or contagion to neighboring countries. With the failure of official financial assistance to restore market confidence, the crises turned into prolonged recessions in many of the affected countries. Ito found merit in much of the criticism of IMF conditionality, especially at the start of the programs.

Looking at the IMF's crisis management in Thailand, Indonesia, and Korea, Ito suggested that "typical IMF prescriptions" did not always have their intended effect and, in fact, may have worsened the situation. A tight fiscal policy may be warranted to enhance confidence and pay for financial reforms. But, Ito said, critics contend, that since Asian countries have a record of sound fiscal policy, such surpluses are not necessary.

The IMF typically recommends tightening monetary policy to prevent further depreciation and inflation. But, Ito noted, critics contend that a sustained high interest rate policy can also lead to a credit crunch or a domestic liquidity crisis.

The emphasis on structural reform in the midst of a crisis was one of the IMF's more controversial conditions, Ito said. For instance, the announcement of the October 1997 program with Indonesia coincided with the forced

Session VI:
The Role of IMF Advice
Chairman: Guillermo Ortiz Martinez, Governor, Bank of Mexico
Paper
Takatoshi Ito, Professor, Hitotsubashi University
Panel
Mohsin S. Khan, Director, IMF Institute
Mario Draghi, Director General, Ministry of the Treasury, Italy
Kiettisak Meecharoen, Assistant Governor, Bank of Thailand
Guillermo Ortiz Martinez

Closing remarks
Stanley Fischer, IMF First Deputy Managing Director

cial sector can and should press further to resist unwarranted movements in major currency exchange rates.

External payments difficulties

The purposes of the IMF's activities in this area are clearly defined in its Articles of Agreement: "To give confidence to members by making the general resources of the IMF temporarily available to them under adequate safeguards. . . ." The objective of "giving confidence to members" applies not only to times of difficulty. More generally, because open policies toward international trade bring public goods benefits to the global economy, it is desirable to persuade members to adopt such policies by offering some assurance of assistance in the event that they encounter external payments difficulties. This argument applies as well to open and prudent policies toward international capital movements, and it is high time for the IMF's Articles to be amended to reflect this.

The constraint that use of the IMF's general resources should be "temporary" and subject to "adequate safeguards" reflects the policy of the international community to be prepared to provide interest-bearing loans, but not grants, to assist countries that are themselves acting constructively, from an international as well as a domestic perspective, to address their own problems. Thus, promotion of the global public good, not merely the correction of disequilibrium in the assisted country, is the clear purpose of the IMF's financial assistance.

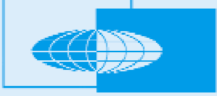
Because the IMF provides loans with firm expectations of repayment, it is not absorbing losses that should be borne by members or their creditors and is thus not contributing directly to problems of moral hazard. Furthermore, through the safeguards built into the IMF's conditionality, members receiving IMF assistance are pressed to reform their policies not only to correct current problems but also to reduce the risk of future payments difficulties. With these reforms, and the continuing efforts to improve the architecture of the international monetary system and involve constructively the private sector in both lessening the risks and ameliorating the effects of financial crises, I am convinced that the problem of moral hazard can be adequately contained.

On the scale of some recent support packages, the IMF has not been alone; important additional support has come from the World Bank, the Asian Development Bank, the Inter-American Development Bank, and from national governments and central banks. Clearly, in these cases, the responsible judgment of the international community was that financial support beyond the substantial amounts provided by the IMF was necessary and appropriate.

On conditionality, initial economic assumptions in several recent programs proved substantially too optimistic, and it was appropriate to exploit the flexibility of program revisions to better adapt economic policies to unforeseen circumstances—in some cases leading from a prescribed initial tightening to a subsequent substantial easing of fiscal policies. For monetary policies, initial tightenings were, in my view, not only the right policies, but absolutely essential to resist what were already excessive exchange rate depreciations with threatening domestic and international implications.

It is a grave mistake to think that there is an easy way out when a country and its government have lost the confidence of financial markets. Countries that have pressed vigorously ahead are beginning to see the fruits of their efforts even earlier than expected. To generate the greatest possible global public good out of the difficulties of the past two years, it is essential to keep the reform process moving forward.

An increasingly open system of world trade and an increasingly and prudently liberalized system of world finance are the two great global public goods that have been produced by the international community in the postwar era. The effort to reform the system is fundamentally the effort to sustain and enhance these public goods.



closure of 16 banks, which caused a run on banks and created an atmosphere of general distrust. Although it is important to identify and close insolvent banks during a crisis, weak but viable banks should be strengthened with government money, if possible, he suggested.

The IMF's position on structural policies, according to Ito, is that they enhance efficiency and equity and avoid inefficient investment that is subject to political influence. A crisis provides a window of opportunity to impose a long-overdue agenda.

Takatoshi Ito raised questions about IMF policy advice to countries hit by financial crisis.

Although the IMF's critics have not disputed the long-run benefits of structural policy reform, Ito said, they have questioned whether a crisis is the best time to introduce reforms that are not specifically related to the balance of payments, even though it may be politically more difficult to implement such reforms during periods of relative calm. When a reform agenda is too long and too tough, investors may react negatively if they suspect that the government will not follow through on implementation.

Discussion. Most discussants were less critical of the IMF's role as crisis manager. Mohsin S. Khan observed that without any IMF action or assistance, the outcome of the crises could have been immeasurably worse. He noted that crisis prediction is difficult in its early stages. Even an accurate early warning system could have little effect if policymakers ignored warnings and markets heeded them.

Mario Draghi said contagion among the southeast Asian countries would have been hard to avoid, since many of them had trade links and competed among themselves. He agreed with the IMF position that interest rates have to be kept high until market confidence returns, and they cannot come down until the right policies are implemented. Reform of the financial sector, he said, was crucial for a country's recovery.

Stanley Fischer noted that the international community is not relaxing its efforts to find effective means of dealing with future crises.

Kiettisak Meecharoen said that the unexpected severity and spread of the Thai currency crisis had washed over the IMF's support and financial assistance. Also, problems in the financial sector were worse than originally thought; the crisis provided an opportunity for the authorities to make sweeping reforms not possible in normal times.

John Williamson was more critical of the IMF's policy advice. The emphasis on excessive fiscal austerity was a mistake, although he acknowledged that the IMF recognized its error and adjusted reasonably quickly. High interest rates, however, might make people question the solvency of the country's institutions and might be interpreted as a panic signal that would do more harm than good. Guillermo Ortiz Martinez said that the relatively quick resolution of the Mexican financial crisis of 1994–95 benefited from early diagnosis and a quickly implemented program. The denial stage, he said, did not last as long in Mexico as it did in Asia. In both cases, strong measures were needed to counter the overreaction of markets.

Concluding remarks

In his concluding remarks, Stanley Fischer focused on three issues:

• *Martin Wolf's suggestion that governments should limit their foreign exchange exposure in capital markets.* Borrowing in the capital markets is healthy for a country, Fischer said; it provides for competition for the domestic economy and for technology transfers. If a country stays closed, its financial system remains underdeveloped. There are problems, of course, but even after suffering serious financial crises, virtually all emerging market economies have opted for openness over capital market autarky. The challenge is to make the world safer in spite of capital market exposure, through, for example, better supervision, transparency, and possibly in some cases controls on short-term inflows.

• *Appropriate exchange rate regime.* Among countries facing currency crises, those that had fixed or pegged rates tended to get hit the hardest when they tried to defend their rate or maintain the peg, Fischer noted. Countries with floating rates that have suffered speculative attacks in the past—Israel, South Africa, Turkey—seemed to have suffered less serious hits. The move toward floating, with prudential controls, will likely continue, although hard currency pegs would also be favored among some countries, such as Argentina.

• *Moral hazard.* This question informs the design of every institution, Fischer said. A safety net was part of the architecture set up in 1945 to enable the IMF to provide comfort to member countries. There will always be moral hazard in an equilibrium. The question that needs to be asked is: How much moral hazard can be contained in a sustainable equilibrium? A crisis is obviously not a sustainable equilibrium, so measures need to be adopted to keep moral hazard within permissible limits. The advanced economies should take the lead in implementing changes, such as "majority clauses" in new bond contracts, which would make it harder for individual bond holders to sue a sovereign borrower.

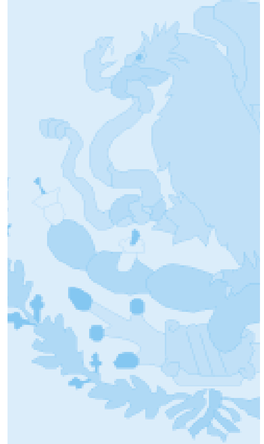
Fischer concluded by noting that, as the worst effects of the Asian crisis fade, the international community is not relaxing its efforts to find new and effective means to deal with future crises, as some critics claimed happened after the Mexican crisis. ■

Sara Kane
Deputy Editor, *IMF Survey*

The IMF will publish the proceedings of this conference later in the year.

$4.1 billion package

IMF Executive Board to consider Stand-By credit for Mexico



In a news brief issued on June 15, IMF Managing Director Michel Camdessus announced that an IMF Executive Board meeting had been set for early July to consider Mexico's request for a Stand-By credit from the IMF equivalent to SDR 3.1 billion (about $4.1 billion). "The credit would be in support of the government's strong economic program for 1999–2000," Camdessus said, "and would help ensure the maintenance of a strong policy framework during the transition to the next administration, and thereby support market confidence during this period.

"Economic growth in Mexico has been resilient in the face of international market turbulence. The government has reacted swiftly to a series of external shocks over the past two years, with adjustments in fiscal and monetary policies. Moreover, the flexible exchange rate has acted as an important buffer, giving market participants greater confidence that no major imbalances would develop.

"The 1999–2000 economic program aims to reduce inflation to 10 percent by 2000. Real GDP growth is projected to slow in 1999, reflecting, in part, reduced access to international capital markets, and then recover to 5 percent in 2000 as market access improves and investment picks up. The authorities intend to maintain tight fiscal and monetary policies and vigorously implement structural reforms that are already in progress.

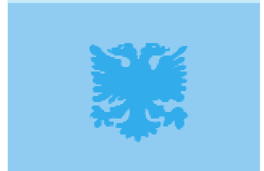
"The overall public sector deficit is programmed, based on a conservative oil price assumption, at 1¼ percent of GDP in 1999, the same level as last year, with a decline to 1 percent of GDP planned for 2000. Fiscal measures already taken are expected to raise non-oil revenue by over ½ of 1 percentage point of GDP, while expenditure restraint is maintained within the context of increased social spending.

"As part of the program, the banking system is to be strengthened. This will be facilitated by financial sector legislation passed in December 1998 that established the Savings Protection Institute, which, among other things, will create an intervention and resolution framework for distressed banks and manage the assets acquired by the Savings Protection Fund. The authorities also intend to continue to enforce strict adherence to existing regulations and upgrade the system's legal, regulatory, and supervisory framework consistent with Basle core principles," Camdessus said.

The text of News Brief 99/29 is also available on the IMF's website (www.imf.org).

$30 million released

IMF Board approves Albania's second annual program and augmentation under ESAF



In a news brief issued on June 14, IMF First Deputy Managing Director Stanley Fischer announced that the Executive Board of the IMF had met that day to assess Albania's request for a second annual arrangement and augmentation of access under the Enhanced Structural Adjustment Facility (ESAF). "The request was approved and, as a result, SDR 21.5 million (about $30 million) is available to Albania during the second annual ESAF arrangement.

"Directors commended the authorities for their success in restoring macroeconomic stability following the 1997 financial disturbances, which were occasioned by the collapse of pyramid schemes. They noted that in 1998, output rebounded from its earlier losses, inflation was significantly reduced, and international reserves were kept at a reasonably comfortable level. Directors considered that this success stemmed from the implementation of prudent macroeconomic policies and continued progress in key structural reforms, despite the formidable challenges resulting from the Kosovo crisis. Directors recognized that the flood of refugees into Albania since the crisis erupted in late March had placed tremendous strains on the social and economic infrastructure as well as on the budget and balance of payments.

"Directors considered that, with sufficient external support, the crisis need not derail Albania's recovery or prove inflationary. Donor financing of Kosovo-related expenses should enable the government to keep within its 1999 fiscal and monetary program targets, while maintaining a robust rate of growth. Directors emphasized the critical role that financial support from the international community would need to continue to play in meeting the costs of the Kosovo crisis. Directors noted that the achievement of the targeted budgetary outcome would provide room for the expansion of private credit under the monetary program, although this expansion would be desirable only if bank restructuring efforts were accelerated and bank supervision practices strengthened. Noting the authorities' prudent

implementation of monetary policy and success in restoring price stability, Directors saw scope for some interest rate cuts in the period ahead.

"Directors stressed that it would be essential to maintain the momentum of structural reforms and efforts to improve governance if rapid growth was to be sustainable. In this connection, recent actions and statements by the authorities were particularly encouraging. Directors urged the government to intensify its efforts to mobilize tax revenues in order to provide sufficient budgetary resources for development and priority social spending. Directors considered that tax revenues could be increased by broadening the tax base, especially through the inclusion of the agricultural sector in the tax net, and by addressing the recognized problems of fraud and corruption in customs administration. Other priorities were to accelerate privatization in the banking and other strategic sectors of the economy and to build on the progress in agricultural land registration in order to foster the land market and consolidate land holdings.

"Directors also stressed that utmost vigilance was needed to ensure that the strains created by the Kosovo crisis did not weaken governance. The government should continue to implement its anticorruption program and necessary reforms in the judiciary, customs, and public administration. The pyramid scheme episode should also be brought to a speedy and transparent conclusion. Finally, Directors stressed that it was critical for the authorities to observe the highest standards of transparency in accounting for expenditures and funding connected with the Kosovo crisis. They accordingly welcomed the authorities' intention to place the financial assistance provided by the donor community in a separate account and to make information on related transactions available to the public.

"Directors reiterated their strong support for the Albanian authorities' adjustment and reform efforts and wished them every success," Fischer said. ■

The text of News Brief 99/27 is also available on the IMF's website (www.imf.org).

Press Releases

Following is an excerpt of a recent IMF press release. The full text is available on the IMF's website (www.imf.org) under "news" or on request from the IMF's Public Affairs Division (fax: (202) 623-6278).

Albania: ESAF

The IMF approved the second annual arrangement under the Enhanced Structural Adjustment Facility (ESAF), and an augmentation of SDR 9.7 million (about $13.1 million) in the amount of resources committed under the arrangement, to support Albania's economic and financial program. The augmentation takes into account Albania's increased balance of payments needs arising from the impact of the Kosovo crisis. The three-year ESAF arrangement was approved on May 13, 1998, in an original amount of SDR 35.3 million (about $47.5 million), of which one-third has been disbursed. (See Press Release No. 98/18, *IMF Survey*, May 25, 1998, page 170.) Today's [June 14] decision increases the total amount of the ESAF arrangement to SDR 45.0 million (about $60.6 million) and triggers release of SDR 9.6 million (about $12.9 million).

Albania: basic indicators and macroeconomic framework

	1996	1997	1998[1]	1999[1]	2000[2]	2001[2]	2002[2]
	(percent change)						
Real GDP	9.1	–7.0	8.0	8.0	8.0	8.0	8.0
Retail prices (during period)	17.4	42.1	8.7	7.0	5.0	3.0	3.0
	(percent of GDP)						
Domestically financed deficit	10.6	10.8	6.4	5.5	4.3	3.3	2.5
Current account balance[3,4]	–9.1	–12.1	–6.1	–11.9	–8.6	–7.2	–6.1
	(months of imports of goods and services)						
Gross international reserves	3.1	4.5	4.7	3.7	3.8	3.6	3.5

[1]Estimates.
[2]Projections.
[3]For 1999, excluding imports of direct humanitarian aid related to the Kosovo crisis.
[4]Excluding official transfers.

Data: Albanian authorities and IMF staff estimates and projections

Medium-term strategy and 1999/2000 program

Albania's program seeks to achieve rapid economic growth, low inflation, greater employment opportunities, and reduced poverty. It requires ambitious and comprehensive structural reforms and a concerted attack on poor governance. After the Kosovo crisis broke out, Albania's authorities continued to focus on maintaining macroeconomic stability and the momentum of reforms. The impact of the crisis on growth and inflation is expected to be small, assuming that refugee-related expenditures are largely financed by the international community. Under the assumption that the refugees will have returned home by early 2000, foreign direct investment resumes, and fiscal consolidation and structural reforms continue as programmed, growth is expected to average 7–8 percent a year, while inflation stabilizes at industrial country levels.

The budget impact of the Kosovo crisis is estimated at $154 million (4 percent of GDP for 1999). However, the authorities aim to ensure that this does not interfere with underlying fiscal consolidation. Albania plans to stick to the original budget goal of reducing the domestically financed deficit to 5.5 percent of GDP in 1999, and about 4 percent in 2000. However, if cuts in essential development and social expenditures are to be avoided, this can realistically be achieved only if the international community finances the large budgetary cost of helping the refugees. Monetary policy for 1999 is designed to meet the inflation and balance of payments objectives and is not expected to be deflected by the Kosovo crisis.

Structural reforms

Albania is determined to keep up the momentum of structural reforms and step up the fight against corruption. Key priorities are to restructure the banking system, extend privatization to the economy's strategic sectors, and strengthen tax collection. Albania aims to continue the significant progress already achieved in establishing a liberal and open trade system through further reduction of tariffs in the next few years.

Albania joined the IMF on October 15, 1991, and its quota is SDR 48.7 million (about $65.5 million). Its outstanding use of IMF financing currently totals SDR 42.0 million (about $56.5 million).

Press Release No. 99/21, June 14

Stand-By, EFF, and ESAF Arrangements as of May 31

Member	Date of arrangement	Expiration date	Amount approved	Undrawn balance
			(million SDRs)	
Stand-By Arrangements			**32,747.02**	**8,428.59**
Brazil[1]	December 2, 1998	December 1, 2001	13,024.80	5,969.70
Bosnia and Herzegovina	May 29, 1998	August 28, 1999	60.60	36.36
Cape Verde	February 20, 1998	December 31, 1999	2.50	2.50
El Salvador	September 23, 1998	February 22, 2000	37.68	37.68
Korea[1]	December 4, 1997	December 3, 2000	15,500.00	1,087.50
Philippines	April 1, 1998	March 31, 2000	1,020.79	633.40
Thailand	August 20, 1997	June 19, 2000	2,900.00	500.00
Uruguay	March 29, 1999	March 28, 2000	70.00	70.00
Zimbabwe	June 1, 1998	June 30, 1999	130.65	91.45
EFF Arrangements			**11,675.43**	**7,599.01**
Argentina	February 4, 1998	February 3, 2001	2,080.00	2,080.00
Azerbaijan	December 20, 1996	December 19, 1999	58.50	15.80
Bulgaria	September 25, 1998	September 24, 2001	627.62	470.72
Croatia, Republic of	March 12, 1997	March 11, 2000	353.16	324.38
Indonesia	August 25, 1998	November 5, 2000	5,383.10	2,259.40
Jordan	April 15, 1999	April 14, 2002	127.88	117.22
Kazakhstan	July 17, 1996	July 16, 1999	309.40	154.70
Moldova	May 20, 1996	May 19, 2000	135.00	72.50
Pakistan	October 20, 1997	October 19, 2000	454.92	379.09
Panama	December 10, 1997	December 9, 2000	120.00	80.00
Ukraine	September 4, 1998	September 3, 2001	1,919.95	1,563.30
Yemen	October 29, 1997	October 28, 2000	105.90	76.90
ESAF Arrangements			**4,176.48**	**2,233.38**
Albania	May 13, 1998	May 12, 2001	35.30	23.53
Armenia	February 14, 1996	December 20, 1999	109.35	20.93
Azerbaijan	December 20, 1996	January 24, 2000	93.60	17.55
Benin	August 28, 1996	January 7, 2000	27.18	14.50
Bolivia	September 18, 1998	September 17, 2001	100.96	84.13
Burkina Faso	June 14, 1996	September 13, 1999	39.78	0.00
Cameroon	August 20, 1997	August 19, 2000	162.12	54.04
Central African Republic	July 20, 1998	July 19, 2001	49.44	41.20
Congo, Republic of	June 28, 1996	June 27, 1999	69.48	55.58
Côte d'Ivoire	March 17, 1998	March 16, 2001	285.84	161.98
Ethiopia	October 11, 1996	October 22, 1999	88.47	58.98
The Gambia	June 29, 1998	June 28, 2001	20.61	17.18
Georgia	February 28, 1996	July 26, 1999	166.50	27.75
Ghana	May 3, 1999	May 2, 2002	155.00	132.84
Guinea	January 13, 1997	January 12, 2000	70.80	23.60
Guyana	July 15, 1998	July 14, 2001	53.76	35.84
Haiti	October 18, 1996	October 17, 1999	91.05	75.88
Honduras	March 26, 1999	March 25, 2002	156.75	96.90
Kyrgyz Republic	June 26, 1998	June 25, 2001	73.38	43.00
Macedonia, FYR	April 11, 1997	April 10, 2000	54.56	27.28
Madagascar	November 27, 1996	November 26, 1999	81.36	54.24
Malawi	October 18, 1995	December 16, 1999	50.96	7.64
Mali	April 10, 1996	August 5, 1999	62.01	0.00
Mongolia	July 30, 1997	July 29, 2000	33.39	27.83
Mozambique	June 21, 1996	August 24, 1999	75.60	0.00
Nicaragua	March 18, 1998	March 17, 2001	148.96	67.27
Niger	June 12, 1996	August 27, 1999	57.96	9.66
Pakistan	October 20, 1997	October 19, 2000	682.38	417.01
Rwanda	June 24, 1998	June 23, 2001	71.40	47.60
Senegal	April 20, 1998	April 19, 2001	107.01	71.34
Tajikistan	June 24, 1998	June 23, 2001	100.30	60.00
Tanzania	November 8, 1996	February 7, 2000	181.59	29.38
Uganda	November 10, 1997	November 9, 2000	100.43	43.52
Yemen	October 29, 1997	October 28, 2000	264.75	140.75
Zambia	March 25, 1999	March 24, 2002	254.45	244.45
Total			**48,598.93**	**18,255.98**

[1]Includes amounts under Supplemental Reserve Facility.
EFF = Extended Fund Facility
ESAF = Enhanced Structural Adjustment Facility
Figures may not add to totals owing to rounding.

Data: IMF Treasurer's Department

Adjustment measures under ESAF-supported programs are expected to strengthen a country's balance of payments position and foster growth.

BIS, IMF, OECD, World Bank release data

Joint debt statistics provide overview of important categories

In March, the IMF, the Bank for International Settlements (BIS), the Organization for Economic Cooperation and Development (OECD), and the World Bank announced the joint publication of the first of a new series of quarterly releases of statistics for 176 developing and transition countries (see *IMF Survey*, March 22, 1999, pages 90–91). In mid-June, the second quarterly release of the Joint BIS-IMF-OECD-World Bank Statistics on external debt was posted on the websites of the contributing organizations. In early July, an on-line data access facility will be included to allow users to download and manipulate time series for each of the data categories covered. This article provides guidance to users to help them interpret the time series presented on the website (see www.imf.org/external/pubs/pubs/per.htm).

The Joint Debt Statistics are an ongoing project of the Inter-Agency Task Force on Finance Statistics, chaired by the IMF, and including members from the BIS, the European Central Bank, Eurostat, the OECD, the United Nations (represented at recent meetings by the United Nations Conference on Trade and Development (UNCTAD)), and the World Bank. The Paris Club and the Commonwealth Secretariat have also participated in recent meetings.

The joint statistics are part of a series of initiatives by the IMF and other organizations to strengthen the international financial system through greater transparency, and the task force is studying further enhancements. In particular, the need for more timely, accurate, and comprehensive information on external debt and international reserves was stressed, including by the Group of Seven and the Interim Committee of the IMF at the political level; by the Committee on Global Financial Systems of the Group of 10 central banks and the Group of 22 Working Group on Transparency and Accountability at the technical level; and by the Institute of International Finance at the level of private market participants.

IMF work has identified weaknesses in existing external debt data—principally, incomplete coverage of sectors, debt instruments, and types of transactions—that limit the ability of policymakers and market participants to assess external vulnerabilities and price risks and to allocate capital across countries. Data on short-term debt and offshore financial centers present additional significant problems.

While the task force was in broad agreement that national debt compilers should be urged to strengthen efforts to remedy these shortcomings, it recognized that, in the short run, creditor source data should be exploited more fully. There was also a broadly shared conviction not only that data should be meaningful and accurate, but that compilers should also explain their methodology and sources. The joint debt statistics attempt to fill these gaps.

Features

Hyperlinking. Labels identifying each of the time series covered are hyperlinked from the joint website to information on their methodological characteristics and sources.

Sources. The joint debt statistics are derived mainly from creditor and market sources. For example, data on borrowing from banks are from creditor positions reported by banks and other financial institutions to the BIS; data on trade credits are collected by the OECD from credit guaranty agencies in member countries; and data on securities are compiled by the BIS primarily from commercial records. Information on Brady bonds is collected by the World Bank from national debt agencies—and not published elsewhere. Similarly, the data on securities positions with a maturity of one year are not published elsewhere.

Timeliness. Data presented in the joint statistics range from two months for securities to nine months for bilateral loans, but, for now, the quarterly releases are synchronized with the publication of the BIS banking statistics, which constitute the principal input into the joint debt statistics and are released five and a half months following the reference date.

Residency principle. Virtually all the data included in the joint statistics are based on the residency principle, which, from an analytical point of view, offers the advantage of facilitating their use in conjunction with balance of payments data. However, domestically issued securities—such as large amounts of securities issued by the Russian Treasury—acquired by nonresidents, are cov-

Members' use of IMF credit
(million SDRs)

	May 1999	Jan.–May 1999	Jan.–May 1998
General Resources Account	**181.25**	**5,205.48**	**6,073.92**
Stand-By Arrangements	181.25	4,194.57	5,036.89
SRF	0.00	3,636.09	3,935.00
EFF Arrangements	0.00	567.79	1,037.03
CCFF	0.00	443.12	0.00
ESAF Arrangements	**50.35**	**380.86**	**421.71**
Total	**231.60**	**5,586.34**	**6,495.63**

Note: SRF = Supplemental Reserve Facility
EFF = Extended Fund Facility
CCFF = Compensatory and Contingency Financing Facility
ESAF = Enhanced Structural Adjustment Facility
Figures may not add to totals shown owing to rounding.

Data: IMF Treasurer's Department

ered by the joint statistics only to the extent that they are acquired by BIS-reporting banks. An additional shortcoming is the assumption that all internationally issued securities are held by nonresidents of the debtor country.

Short-term banking data. The short-term banking data from the BIS's consolidated banking statistics, as well as securities positions, are presented on a residual one-year basis, instead of an original maturity basis. This may be helpful for assessing countries' external vulnerability.

Off-balance-sheet items and offsetting financial assets. Two important issues that have complicated the analysis of debt data are off-balance-sheet items and the impact of offsetting financial assets relating to the concepts of external vulnerability and "net" debt. Offsetting assets are addressed, in part, by the inclusion of information on international reserve assets in the joint statistics. The external debt data presented here and in most other publications are not a substitute for data on the International Investment Position, which, based on the IMF's *Balance of Payments* Manual (Fifth Edition), presents the complete balance sheet of the stock of external financial assets and liabilities. The IMF's Special Data Dissemination Standard recognizes the importance of the International Investment Position by prescribing the dissemination of annual data for it and encouraging quarterly data.

The joint statistics do not provide information on off-balance-sheet items—with some exceptions for trustee business—such as derivative financial instruments or guarantees, which may alter the extent of the external vulnerability of countries. The compilation of statistics on off-balance-sheet items is being studied by the Inter-Agency Task Force on Finance Statistics. Other "on-balance-sheet" instruments—financial leases, subordinated loans, and intercompany loans other than interbank positions—are covered only for positions vis-à-vis BIS reporting banks by the joint debt statistics and continue to constitute significant gaps.

Developed country data. Currently, the joint debt statistics do not present data for developed economies, which might reinforce the erroneous notion that external debt issues concern developing nations and emerging markets only. Discussions are under way to expand the coverage of the joint debt statistics to include all countries. Also, the joint debt statistics devote a special section to offshore financial centers.

Nonbank trade credits. The data on nonbank trade credits cover official and officially guaranteed credit only, which, depending on the type of country for which the data are reported, may underestimate the coverage more or less significantly. Similarly, to improve the timeliness of the data, the multilateral category covers IMF and World Bank credits only—whose effect on individual country data may vary significantly. Improvements in this area are under discussion.

Source comparisons. Comparisons between external debt data based on debtor and creditor sources show differences that are more or less significant for individual countries. Some of the differences are related to shortcomings of the debtor source data, but creditor and market source data are also subject to shortcomings.

While the joint debt statistics add some value for analysts, the data essentially provide an overview of important debt categories for the countries concerned. Significant gaps and overlaps remain, which explains why the contributing agencies have chosen not to present total debt aggregates as part of this publication. ■

Jan Bové, IMF Statistics Department

Photo Credits: Denio Zara and Padraic Hughes for the IMF.

IMF Appoints Dawson as External Relations Director

IMF Managing Director Michel Camdessus has named Thomas C. Dawson II, a Merrill Lynch and Company executive and former IMF Executive Director, to the post of Director of the IMF's External Relations Department. Dawson, who will formally assume the post on August 2, succeeds Shailendra J. Anjaria, who has been named Secretary of the IMF (see Press Release No. 99/18, *IMF Survey*, June 7, page 178).

Dawson, a national of the United States, will become Director Designate of the External Relations Department on July 1 as part of the transition within the IMF department responsible for media relations, private sector affairs, relations with civil society, and publications activities. His appointment is for a three-year term.

Dawson is currently a Director in the Financial Institutions Group of Merrill Lynch in New York. In this position, he has been responsible for the firm's relationships with the IMF, the World Bank, and other multilateral institutions.

Prior to joining Merrill Lynch in 1993, Dawson served for four years as the Executive Director for the United States at the IMF. He was also responsible for representing the United States in numerous international financial negotiations, including dealings with the private sector. In 1981, he was named Deputy Assistant Secretary for Developing Nations at the U.S. Department of Treasury, and was named Assistant Secretary for Business and Consumer Affairs in 1984. He served between 1985 and 1987 in the White House Chief of Staff's office.

A U.S. Foreign Service Officer from 1971 until 1976, Dawson was employed by McKinsey and Company as a consultant focusing on international business and investment strategy from 1978 to 1981.

He is a native of Washington, DC, and holds a bachelor's degree in economics and a master's degree in business administration from Stanford University.

Press Release No. 99/22, June 16

Bretton Woods institutions adapting to meet needs

(Continued from front page) economy would depend on developing mature relationships between borrowers and lenders and on the ability of all participants to lay the basis for successful crisis resolution before crises strike.

The question of the IMF's obligations in this new world of international finance was also at the heart of the panel discussion on how best to meet the general resource needs of the IMF in the future. While Adam Lerrick contended the IMF should tap private markets, Jessica Einhorn raised several serious concerns, among them fears of unacceptable conflicts of interests for the IMF in a period when it is increasingly called upon to assume a growing role in regulating private international finance, particularly in crisis situations.

It was clear, Rubin said in his keynote address, that nothing should be taken for granted. As the 1990s have vividly demonstrated, the global economy can provide considerable risks as well as extraordinary opportunities. The Bretton Woods organizations must adapt to meet globalization's challenges, but, more broadly, supporters of a market-based international economy and an open trading system must make certain the benefits of an integrated global economy are widely shared and better understood, so that its goals continue to draw political support.

World Bank and IFC look ahead . . .

Press preoccupation during the Asian crisis with financial packages, exchange rates, economics, and statistics "made us humble," World Bank President James Wolfensohn said. The experience prompted the Bank to reorder its priorities and increasingly shift its focus to structural issues, so that it could address, among other things, the need to confront corruption and promote good governance; to ensure viable legal and judicial systems to allow private sectors to thrive; to develop effective supervisory and regulatory agencies for financial systems; and to help design social safety nets for economies in crisis and in transition.

Wolfensohn: The World Bank is increasingly shifting its focus to structural issues.

The Bank will not be able to do all this on its own, Wolfensohn acknowledged, and there will be much more coordinated work with the international financial institutions, the nongovernmental organizations (NGOs), civil society, and the private sector. These are not the types of measures to grab headlines, but the Bank's new focus on structure is the correct one, he believed.

Peter Woicke, who became Executive Vice President of the International Finance Corporation (IFC) and Managing Director of Private Sector Operations for the World Bank Group on January 1, 1999, addressed a luncheon gathering of committee members. He sketched for them his plans for the organization in the coming years, focusing on the work of the World Bank Group and private sector development.

IMF and "bailing in" the private sector

If any characteristic distinguishes this decade's economic crises, Camdessus observed, it has been the prominent role played by private sector creditors and debtors. As the Mexican and Asian crises pointedly confirm, market players, regulators, and policymakers failed to fully grasp the risks that accompanied the decade's considerable opportunities.

While the search is still on for the causes and cures of these crises, the principle underlying any remedy must be, Camdessus said, the "need to foster a mature market" based on stable relationships among participants. Official involvement should be limited, he said, "to establishing strong legal, regulatory, and supervisory frameworks," and the value of good governance, transparency, and cooperation should be apparent to all.

But what specifically, Camdessus asked, could debtors, creditors, and the IMF do? For debtors, he noted that honoring contracts is the foundation on which mature markets are built. But to this basic step must be added macroeconomic stability and growth, a workable bankruptcy law and an independent judicial system, adherence to international standards of disclosure and governance, development of a robust regulatory and supervisory framework for the financial sector, and promotion of sound debt management and frequent monitoring of private external liabilities.

For creditors, risk assessment and risk management are the chief concerns, but creditors should also encourage adherence to international standards and be willing to support adaptations of regulatory and supervisory standards in their own countries, according to Camdessus. Private creditors can also help preserve foreign exchange liquidity by providing contingent financing when crises loom. Good communication between creditors and debtors will, of course, be an essential ingredient in any mature relationship.

Selected IMF rates

Week beginning	SDR interest rate	Rate of remuneration	Rate of charge
June 7	3.31	3.31	3.76
June 14	3.35	3.35	3.81

The SDR interest rate and the rate of remuneration are equal to a weighted average of interest rates on specified short-term domestic obligations in the money markets of the five countries whose currencies constitute the SDR valuation basket (as of January 1, 1999, the U.S. dollar was weighted 41.3 percent; euro (Germany), 19 percent; euro (France), 10.3 percent; Japanese yen, 17 percent; and U.K. pound, 12.4 percent). The rate of remuneration is the rate of return on members' remunerated reserve tranche positions. The rate of charge, a proportion (currently 113.7 percent) of the SDR interest rate, is the cost of using the IMF's financial resources. All three rates are computed each Friday for the following week. The basic rates of remuneration and charge are further adjusted to reflect burden-sharing arrangements. For the latest rates, call (202) 623-7171 or check the IMF website (www.imf.org/external/np/tre/sdr/sdr.htm).

Data: IMF Treasurer's Department

The IMF's traditional activities—notably, bilateral and multilateral surveillance—offer the first line of its defense of a stable international economy. But a recent IMF innovation—the creation of Contingent Credit Lines—now also allows it to offer financial resources to bolster those crisis prevention efforts.

But, as Camdessus acknowledged, crises will happen, and a "delicate balance" must be maintained among the objectives of preserving countries' market access in normal times, ensuring equitable treatment of creditors if a crisis strikes, and avoiding debtor and creditor moral hazard through market-based and market-friendly solutions. Where new financing is not available and comprehensive debt restructuring is needed, he argued that bondholders should not expect public funds from the international community to shield them. In some extreme cases, he said, countries may have no orderly way out of the crisis without a comprehensive debt restructuring that includes bonds. Where default cannot be avoided, it will be critical to maintain proper working relations and avoid having good faith negotiations stymied by a handful of dissident creditors. One option—admittedly a controversial one, he said—would be to require a new interpretation or amendment of the IMF's Articles of Agreement to allow the IMF to declare a stay on legal actions of creditors during such negotiations. But if all concerned take the necessary steps to develop a mature relationship, these extreme cases would be rare and the framework would be in place to deal with them, according to Camdessus.

Should the IMF use private financing?

Private Sector Financing for the IMF: Now Part of the Optimal Funding Mix, a study published by the Bretton Woods Committee, provided the basis for a panel discussion among Adam Lerrick, author of the study and head of an advisory firm focused on funding strategies and structured finance; Jessica Einhorn, a Visiting Fellow at the IMF and previously a Managing Director at the World Bank in charge of financial management and resource mobilization; and Thomas C. Dawson II, Director of Merrill Lynch's Financial Institutions Group and incoming Director of the IMF's External Relations Department (see page 205). They found themselves sharply divided on the key question of whether private financing was in keeping with the character and objectives of the IMF.

Lerrick presented a summary of his report's findings, arguing that the world economy, the markets, and the nature of the IMF's operations had all changed dramatically in recent decades and that the manner in which the IMF financed its operations should adapt accordingly. Recourse to global capital markets, he said, could augment IMF resources by $100 billion, or 50 percent. These additional resources would be available to borrowers at a cost equivalent to current subsidized rates and would provide substantial savings for the IMF's three largest creditor countries—the United States, Germany, and Japan.

For member countries, tapping private capital would "enhance the liquidity and safety of international reserves and underwrite the exchange of zero-cost domestic currency promissory notes for excess reserve positions at the IMF." And for the IMF, he said, tapping private capital would afford flexibility and speed in crisis financing and sidestep political factors within member countries. "The very fact of a major accessible source of alternate funding will moderate the uncertainty that leads to speculation and destabilizes markets," he added.

Adam Lerrick

Einhorn complimented Lerrick on laying out in technical detail the operational aspects of his proposal but argued that the evolution under way in financial architecture in the aftermath of the Asian crisis made market financing for the IMF unthinkable in the foreseeable future. She challenged the cost advantages to the United States of private financing and underscored that profitable investment and currency translation through swap markets—two advantages highlighted in the Lerrick study—would be available only with substantial credit exposure by the IMF to the banking system.

Her basic objections, however, were on principle and unequivocal. "Under all circumstances I can imagine," she said, "I would prefer to see the IMF consigned to managing within its present quota base than permit a market borrowing program." She concentrated her arguments on the public policy side, laying out why Lerrick's proposal "was privately feasible but publicly inappropriate to the quasi sovereign status of the IMF."

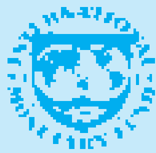
Jessica Einhorn

The design of the IMF—and its reliance on currencies exchanged with members in times of crisis—is critical to its whole mission, she emphasized. The proposal had the IMF holding its prudential liquidity in the banking system in times of crisis. While overall liquidity would remain unchanged by IMF actions, she expressed concern that the IMF would find itself intimately involved in banking exchanges when it should be mediating those calls through major shareholders and their central banks.

Thomas C. Dawson II

She also pointed out that the moral hazard concern—one of the chief criticisms leveled at the IMF—would be exacerbated if the IMF were to have ready access to private money and if private financiers funded both the IMF and the developing countries—and profited from the spreads as well.

Dawson, also underscoring public policy concerns, noted that while he did see some potential scope for private financing of the IMF's Contingent Credit Lines,



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he believed the Lerrick report overstated the benefits of private financing and understated the real problems, notably that the IMF really is "something like a central bank" and does have regulatory responsibilities that are likely to grow. He feared the report was unduly preoccupied with U.S. funding problems. The political difficulties that accompany the quota exercise in the United States are not a problem elsewhere, he said.

Rubin: The politics of international economic policy are as important as the policy.

Opportunities and risks

In a closing address to the Bretton Woods Committee and in what he referred to as one of his last speeches as U.S. Treasury Secretary, Rubin reminded his audience of the tremendous opportunities afforded by the global economy and of the considerable risks that accompanied this process. Recent turmoil in world markets has intensified debate over whether nations should retreat from global integration and market-based economics.

While Rubin had unquestioned faith in the benefits of both, he cautioned supporters of a market-based global economy to heed the anxieties being expressed and the possible erosion of support for global integration and market-based economics. Creating "the conditions in which free flows of capital and market-based economies work best" will entail a number of steps:

• *Strengthening and reforming the international financial institutions.* These institutions have played a critical role in confronting the global financial crisis and have recognized the need to improve their operations and broaden the scope of their concerns. Increasingly, he added, they are more open and promote private sector development; focus on environmental, health, education, labor, human rights, and women's issues; acknowledge the key obstacle that corruption represents; and seek new means to deal with financial crises.

• *Reforming, in a comprehensive manner, the architecture of the international financial system.* This encompasses promoting the adoption of international standards and best practices among developing countries and encouraging better risk management in industrial country financial institutions.

• *Continuing to press for an open trading system.* Rubin expressed deep concern about the recent passage, by the U.S. House of Representatives, of a bill imposing quotas on steel imports. This legislation, "inconsistent with World Trade Organization standards and antithetical to open, market-based economic growth," creates a "real risk of strengthening the already increased protectionist pressure being felt around the world," he said. But those who support free trade also need to recognize that an open trade policy must be complemented by a "forward-looking domestic policy" that gives people the tools to succeed in a global economy and enables those dislocated by the global economy to reenter that economy as quickly as possible.

Rubin also emphasized that the politics of international economic policy were as important as the policy. "We must focus," he said, "on working to broadly share the benefits of growth and globalization, including through bilateral and multilateral aid; targeting resources to the most vulnerable; and offering debt relief to the poorest nations that are committed to reform." These measures, he added, are not just good economic policy, they are key to building support for that policy. ■

Sheila Meehan
Senior Editor, *IMF Survey*

Available on the web (www.imf.org)

News Briefs

99/26, June 7. IMF Executive Board Completes Indonesia Review and Approves $450 Million Credit Tranche

99/28, June 7. Joint BIS-IMF-OECD-World Bank Statistics on External Debt [see page 204, this issue, for a related article]

99/30, June 16. IMF Executive Board Completes Bolivia Mid-term Review

99/31, June 16. IMF Executive Board Completes Thai Review and Approves Next Credit Tranche

99/32, June 16. IMF Executive Board Approves Mongolia's Second Annual Program Under ESAF

Public Information Notices (PINs) are IMF Executive Board assessments of members' economic prospects and policies issued following Article IV consultations--with the consent of the member--with background on the members' economies; and following policy discussions in the Executive Board at the decision of the Board. Recently issued PINs include

99/45, Sudan, June 3
99/46, Vietnam, June 8
99/47, Cape Verde, June 14

Letters of Intent and Memorandums of Economic and Financial Policies are prepared by a member country and describe the policies that the country intends to implement in the context of its request for financial support from the IMF. Recent releases include

Burkina Faso, Letter of Intent, April 16
Cape Verde, Letter of Intent and Memorandum of Economic and Financial Policies, April 26
Argentina, Letter of Intent, May 10
Ukraine, Letter of Intent, May 20
Bulgaria, Letter of Intent, May 28