Navigating Stormy, Uncharted Waters

Five Addresses

by

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Washington, D.C.
October 1998

ISBN 1-55775-762-3

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Foreword

After many years of extraordinary sustained growth, economic crisis spread rapidly through several Asian countries starting in the second half of 1997. Other countries throughout the world were affected in varying degrees by the initial aftershocks. New crises developed, the most severe of which was in Russia. Contagion again affected economies throughout the world, including Latin America, even though many countries there had taken decisive policy measures in the wake of the earlier Mexican crisis. Even the financial markets in the industrial countries were not immune from volatility, despite the underlying strength of activity in these economies.

So the IMF, as well as its membership, is now in stormy, uncharted waters. The events of the past year not only have highlighted the challenges posed by the new "global economy," but also have compelled policymakers around the world to reconsider their agenda for action. The urgent tasks of restoring stability to crisis-ridden countries have been accompanied by other more far-reaching questions. What has gone wrong? Can such crises be anticipated and, even better, averted? If crisis strikes, how can the adverse impact on the people, especially the poorest, be mitigated? What steps need to be taken to ensure that the benefits of globalization can be realized without suffering from periodic crises in vulnerable countries? How can a more robust international economy be built?

The five speeches included in this collection cover a broad range of our activities and thinking over the past year. The themes range from immediate crisis management to the broad questions of a new architecture for the global economy; and from the specific concerns of individual countries and regions to the conditions for a strong and equitable world economy.

The first, most recent speech, delivered in September 1998, steps back from prevailing worldwide market turbulence, seeking lessons from the crises, and stressing that conditions vary extensively among emerging economies. Clear, calm analysis is essential by market participants to differentiate among economies. While crisis has developed in or threatens other regions, in several countries

in Asia it is possible to detect the first signs of recovery, however tentative or incomplete. Although the loss of output and social costs have been more pronounced than was expected, their external financial situation has improved, a first sign that renewed sustainable economic growth may be in prospect.

The second speech sets out initial thoughts not just on the key elements of a new financial architecture, but also on the role that can be played by each constituency in the world economy. It has three themes. First, all countries should recognize the universal benefits of an integrated global economy and increasingly open, liberal capital flows. Second, to minimize the risks, governments and private participants in the market need to subscribe to some basic rules: transparency, good governance, and standards or codes of best practices in a wide range of economic and financial activity. Third, the international organizations themselves, including the IMF, should be adapted and supported to enable them to fulfill their part in managing the global economy.

The remaining speeches elaborate some of these themes. Good governance, a crucial feature of the new architecture, was the theme of an address in Paris in January 1998. Broad institutional, indeed political, issues are raised that illustrate just how far the IMF has come from its traditional focus on short-term macroeconomic stabilization.

Remarks in Kuala Lumpur, delivered in the earlier stages of the crisis in Asia, considered the immediate causes of the turbulence, the responses available to governments, and the steps needed to restore confidence. Already, the ideas of a new financial architecture were taking shape, and they were to assume increasing importance in the thinking of policymakers around the world in subsequent months.

Although inevitably affected by developments in the rest of the world, many countries in Africa continue a quiet resurgence. In an address to the Heads of State of the Organization of African Unity, I reflected on the determined action needed to keep this growth alive: by the countries themselves, by bilateral donors, and by multilateral institutions. For the IMF, the past year provided an opportunity to evaluate our concessional lending window, the Enhanced Structural Adjustment Facility (ESAF), and to observe early results from our joint initiative with the World Bank for the highly indebted poor countries.

The events of the past year did more than reveal the risks that come with globalization. More importantly, they pointed to the need for solutions based on a concerted effort by the international community. Policies, practices, and institutions must be adapted if we are to achieve quality growth in a sound and stable financial environment. These will be the cornerstones of a new financial architecture to face the challenges of the new millennium.

Michel Camdessus
Managing Director

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Crisis in Emerging Market Economies: The Road to Recovery

In a world that becomes more global every day, in a world where private business every day plays an increasingly dominant role in innovation, investment, financing, and ultimately human progress, let me tell you how much I appreciate the opportunity to address this transatlantic business council. Of course the timing of your meeting could not have been more appropriate.

We are witnessing wave upon wave of tensions in global financial markets, turbulence that spreads like wildfire from one part of the world to another. Have economic fundamentals changed so suddenly, so substantially, and simultaneously throughout the world? Or is the loss of confidence that was understandable in some, I repeat, *some* countries, being transferred indiscriminately to all markets, emerging and established alike?

In this volatile situation, calm analysis is more important than ever, remembering that not all markets, not all economies, not all crises, are the same. Nor will the path to recovery, where recovery is necessary, be the same in each case. Market participants—indeed, all of us—need to be discerning, capable of discriminating among economies, aware that when risks turn to reality in one economy, the same course of events does not need to unfold elsewhere, but that all countries, all institutions must read the markets' messages properly.

Let me start by observing that not all the news of the day is gloomy. Although downside risks have increased in recent weeks in so many places, it should be remembered that the fundamentals of the European and North American industrial economies remain sound. The growth of the U.S. economy is continuing in 1998 without inflationary pressure. A recovery in continental Europe has gained momentum, aided by the imminent birth of the euro.

Address to the European-American Business Council, New York, September 15, 1998.

These economies offer a powerful message to the rest of the world, which remains valid even in turbulent times. *Fiscal discipline, supported by a responsive monetary policy within a sound financial system, works.* In North America, long-standing budget deficits are turning to surplus, while in Europe the self-imposed discipline of the convergence criteria under the Maastricht Treaty have brought down deficits, many of which seemed entrenched at much higher levels only a short while ago.

By recognizing yesterday that the balance of risks has shifted from inflation to slowdown in demand, the President of the United States here in New York and ministers of finance and central bank governors of Europe and North America, in the context of a Group of Seven declaration, have indeed pledged their commitment to preserve or create conditions for sustainable domestic growth and financial stability, so critical in today's world environment. So we are at a moment when a credible pro-growth strategy is taking shape—quite a good signal for the world indeed.

Mr. Chairman, you have asked me to focus my remarks tonight on Asia, certainly not because we should downplay the difficult conditions in other parts of the world, but because Asia offers the first rays of hope for resolving the economic crises that now threaten so many countries. In Asia, we find the first countries to experience crisis in 1997, the first to respond, and, although it is not yet widely recognized, the first to be showing some positive results, however tentative and incomplete. The experience of these countries holds out clear hope that serious problems can be avoided in most countries and that seemingly intractable problems in other countries, even Russia, can be resolved given commitment, sound policies, and a steady nerve. This will bring us then to a kind of journey around the world—from Asia to Russia and then to Latin America—concluding by asking ourselves what kind of a new international monetary system could emerge from the present crisis.

* * *

Asia! The origins of its crisis lie in a complex interplay among domestic macroeconomic, structural, institutional, and political factors, strongly connected with developments in the advanced economies and global financial markets.

Reflection on the pre-crisis situation in the Asian countries in mid-1997 points to the buildup in all countries of serious structural problems in the financial and corporate sectors, and to a varying extent, inadequate macroeconomic policies, perhaps most markedly in Thailand, where the crisis started. Overheating, arising from surging private sector demand, was reflected in real estate and stock market bubbles and, in Thailand particularly, in large trade deficits. Pegged exchange rate regimes had been maintained for too long, encouraging heavy external borrowing, including increasing amounts of short-term credit, which created excessive exposure to foreign exchange risk in both the financial and the corporate sectors. Inadequate prudential rules and supervision allowed the quality of banks' loan portfolios to degenerate quickly.

It would not be appropriate, nevertheless, to attribute the financial crisis in Asia, or indeed in other regions, solely to their policy shortcomings. Conditions in international markets are also highly germane. Private investors were attracted by the high returns in these countries, and there perhaps less inclined to assess carefully the risks, as the track record of these countries seemed to make them less risky than most. This led many to lose sight of the fact that the steady appreciation of the dollar against the Japanese yen from mid-1995 was contributing to a loss of export competitiveness in countries whose currencies were tightly linked to the U.S. dollar. Then the Thailand crisis blew up and its depth led the markets to reassess emerging markets' risks—a major factor in the broadening of the crisis. The IMF was called for help . . . always too late indeed.

* * *

The policy programs to respond to crisis in Asian countries had to be speedily designed, to put the proper emphasis on the immediacy of macroeconomic adjustment, and to recognize the sheer magnitude of the structural reforms that had to be initiated from the outset. As a matter of fact, the importance of the structural element is the hallmark of these programs. Within these programs, we can discern three tiers of recovery:

- The first tier is to *restore stability*. As usual, immediate action is needed for countries faced with sudden acute pressure on their balance of payments;

- The second tier is to *improve soundness*. Lost confidence, especially in domestic financial and corporate systems, has to be restored through fundamental institutional changes;
- The third tier is to *boost efficiency*. The approach of "managed development" underlying economic policy, characterized by mechanisms that interfered with market allocation of resources, has become increasingly out of tune with the rigorous demands of our globalized economy. Basic changes in the approach to policymaking, allowing market forces to operate more freely, will be essential. This tier perhaps has been the more controversial due to many misunderstandings on what were at an earlier stage the parameters of the "Asian miracle," and more than that, due to the fact that questioning this approach was tantamount to challenging many vested interests.

Let us take stock of the major programs supported by the IMF in Korea, Thailand, and Indonesia in terms of these three tiers of recovery. First, with respect to the initial stabilization, as so often is the case, it is the bad news that attracts the headlines. There have been setbacks. Economic activity has contracted sharply, more so than was expected at first. This has been the consequence of a sharp drop in investment as financing has been constrained and unprofitable or inefficient projects had to be cut back. A second factor was the "wealth effect" following sharp declines in stock market prices and exchange rates. A third factor was the fall-off in intra-regional trade, especially with Japan, where stagnation has turned to recession during 1998. This crisis at the heart of the region has been of course central to the difficult process of recovery.

With these contractions have come the social costs: an increasing incidence of poverty, rising unemployment, and steeply rising food prices. But programs have been adapted in response. Let me put some emphasis on this point. These programs have not relied primarily on "traditional" prescriptions of budgetary austerity. Except in Thailand, the initial fiscal adjustment called for was quite small, particularly in order to leave room for financial sector restructuring. Moreover, where necessary we have been perfectly ready to alter—yes, to relax—targets to allow room within public expenditure for targeted programs of poverty alleviation and to stimulate the economy. Indeed in more than one country, the IMF actually had to ques-

tion the budgetary zeal of the authorities, exhorting them to make more room for social expenditures.

With respect at least to Thailand and Korea, behind these dark clouds, the beginning of a silver lining can be detected. Several developments point to the return of more stable financial conditions that are essential prerequisites for resumed growth, although undoubtedly new risks arise from recent weakening of the external environment:

- The external position has strengthened decisively. Current accounts have swung sharply from unsustainable deficit to large surplus and international reserves now exceed pre-crisis levels. The main factor has been a steep fall in imports. But exports have also played a large part and the improvement would have been greater if commodity prices had not fallen steeply, and demand from within the region, especially Japan, had not fallen off.
- Currencies are rebounding. After the initial precipitous depreciation, all the currencies of the crisis-ridden countries have shown some appreciation. Even Indonesia, where the decline was steeper and lasted longer, has seen a pronounced appreciation since the depths of its crisis in mid-June. And in Korea, some questions are even being asked about whether the won is appreciating too quickly.
- Interest rates are easing. In Korea, Thailand, and the Philippines, interest rates have declined notably as currency pressures have eased. As monetary conditions ease, the prospects for recovery in demand and output are improving.
- Inflation has not risen as much as had been feared. Although this reflects very weak demand conditions and a decline in real wages, it means that inflation is unlikely to represent an obstacle to resumed growth.

The objective of the second tier of recovery for which we are working in close cooperation with the World Bank and the Asian Development Bank is to promote the changes that would justify renewed confidence in the soundness of both financial and corporate systems.

In the financial sector, banks were brought under greater scrutiny, with the weakest being closed or restructured, sometimes with public funds. Prudential regulations are being strengthened; so

too are standards for accounting, auditing, and disclosure. A more liberal attitude is being taken to foreign banks. The list of changes could be much longer.

The problems of financial systems were in very large measure an outgrowth of fundamental weaknesses in the corporate sector, especially the excessively close relationship between banks, corporations, and the state. This led to an unsustainable situation. So concepts such as transparency, governance in both public and private sectors, and the fight against corruption, have come to center stage. Early on, steps have been taken to work out the massive debt obligations of corporations in a way that is fair to both domestic and foreign creditors. The next stages, already under way, will consist of liberalizing domestic markets, lowering trade barriers, privatization, easing restrictions on entry by foreign investors, and strengthening bankruptcy laws and procedures. But again, time and steadfast implementation will be necessary for results to become evident.

The third tier of recovery will be to increase overall economic efficiency or productivity. For years the Asian tigers' growth was driven significantly by the massive flow of investment, supported by the impetus from an expanding, and increasingly educated labor force. Looking to the future, we can be quite certain that it will not be back to "business as usual." True, many familiar features will still be there: the dynamism, the skilled work force, and the traditional Asian propensity to work and save. Nevertheless, capital may well be less abundant or more costly, so that to restore growth to sustainable levels, investment will have to become much more efficient.

Where are we now? Despite the sharp decline in output, there are promising signs of a good start to the "first tier" of policies. Indeed, if the IMF's mandate were interpreted in a very narrow, traditional sense, as some have suggested it should be, could we not count our task as largely complete? After all, external reserves have been rebuilt, exchange rate stability is being restored, and inflation is at quite low levels. But to stop at this point would not discharge our responsibilities to the countries in crisis or to the world. Only by implementing policies at the second and third tiers, structural and institutional reforms, will it be possible to ensure that the prospects for sustained high-quality growth are restored, that sound institutions and practices are in place, that the external position remains viable in the medium to long term, and, in a word, that the job is done. The

Asian countries in crisis have understood that and the IMF has been willing to offer such large financial assistance precisely because they were willing to adopt policies that went far beyond simple stabilization. This is still a matter of some controversy. You will hear perhaps that we are too ambitious; I will suggest to you that it would be illusory to believe that there could be any other way to solve these deeply rooted problems in a sustainable fashion.

* * *

I will dwell no more on these first three victims of the crisis and our three tiers of strategy for them. But let me turn more briefly to a number of other countries or regions that have been the subject of particular concern in recent weeks as financial pressures have intensified.

Japan first, as it must be central also to the solution of the Asian crisis. Japan, as the second largest industrial economy, plays a pivotal role in the world economy, especially in supporting recovery in Asia. At present, we see an economy that is wracked with financial and corporate sector problems, not so different either from those elsewhere in Asia. But its current recession stands in contrast with the imbalances created by years of fever-pitched activity in the Asian "tigers." In that sense its task is clearer: prompt, resolute action to get its financial system into order is the first urgent order of business. That confidence-building step is essential to underpin the strong fiscal action it may, and indeed should, take simultaneously to stimulate its economy, while pushing its agenda for deregulation, openness, and structural reform.

In *Russia,* the problems are profound; they have origins far beyond the purely economic domain. In economic terms, the principal causes of the Russian crisis relate to domestic fundamentals; contagion from crises elsewhere—including the impact of lower oil and gas prices—is only part of the story. As a matter of fact, even if in a totally different context, the problems of Russia at the beginning of 1998 were strikingly similar to those which at that very moment were destroying Asian prosperity.

Let me tell you a sad anecdote. In early 1998, back from one of my many trips to Asia, I stopped in Russia to confer with President Yeltsin, and others in economic leadership, to share with them some

of the lessons that were already emerging from our experience in East Asia. I told them that a firm monetary stance might well go a long way in stabilizing exchange markets, but that it was neither desirable nor feasible to rely on monetary policy alone for any extended period of time. It was urgent to tackle decisively in Russia the three factors of the "Asian syndrome" that it was also suffering from: continuing macroeconomic deficiency—in Russia, particularly in fiscal policy—weakness in the banking sector, and the pervasiveness of "crony capitalism." It was another way, using the Asian experience, of restating the priorities we had been insisting on for six years. Now, six months later, the markets have delivered their harsh judgment on Russia's failure to address any of these critical issues with sufficient effectiveness. Yes, programs have been ambitious and comprehensive; but implementation fell short.

The path to recovery in Russia will need programs at least as comprehensive as those in Asia, containing elements from all three tiers of policies. Russia's path to recovery is likely to be quite difficult, since Russia needs to restore confidence severely weakened by its decision to unilaterally restructure its domestic debt obligations. Nevertheless, if Russia, like Asia, can begin again to help itself, and do so convincingly, then we stand ready to help. Russia has achieved a lot during the last six years; by far most of the basic elements of its transformation are still in place. Let us hope that the new government will be able soon to start building on these foundations and assembling in the State Duma and in public opinion the broad support that the needed changes will require.

In the meantime, we must continue to shelter the other countries in transition against contagion phenomena. This applies particularly to *Ukraine,* where despite deteriorating conditions in neighboring Russia, the authorities are showing themselves willing to act, committing to significant reform, and adapting their policies in response to changing conditions. Their recent commitments convinced the IMF that it was appropriate to proceed with a new lending program to support Ukraine's reform program. A three-year arrangement was approved a few days ago, with commitments from our side of more than $2 billion.

Let's now cross the Pacific Ocean. Emerging markets in *Latin America* have been particularly affected by market turbulence after the Russian crisis. This region had responded strongly to the

Mexican crisis in 1995, and made significant progress with structural reforms, especially in the area of public finance, and the financial system. In many cases, their economic performance, with a return to low inflation—often in the single-digit range—and stronger external positions, attest to the success of these policies. The region had generally been coping well with the contagion that followed the Asian crisis in 1997. But with global market volatility in recent weeks, coincident with declining oil and primary commodity prices, a number of these economies have come under renewed pressure.

The countries' response to these developments illustrates two points: first, their determination to undertake appropriate policies; and second, the role that the IMF can play in assisting countries on a regional basis through its policy advice, even before any kind of financial assistance. At my invitation, building upon earlier regional meetings, finance ministers and central bank governors from key countries in the Western Hemisphere attended a regional surveillance meeting in Washington 10 days ago. While stressing that they were not seeking additional financial assistance, the authorities attending the meeting reaffirmed that they were committed to sustaining growth through the pursuit of macroeconomic stability, maintaining open capital markets, and deepening reform efforts. As market pressures intensified in subsequent days, these countries took courageous steps to defend their economies. I need hardly say that these are not the statements or actions of countries about to reverse the positive direction of economic policies. Nor are they the statements of countries that pursue irresponsible economic policies assuming that they will be "bailed out" by the IMF. Nevertheless, it is proper to add that, as I declared last Friday with the unanimous backing of the IMF's Executive Board, the IMF already has financial arrangements with several countries in Latin America, and according to its mandate, it stands ready to strengthen its financial support and broaden it to other countries, if necessary, to back strong economic programs.

In contrast with this policy stance, I must recognize that there are still, from time to time and from place to place, voices to recommend to countries confronted by a difficult external environment that they yield to the temptation of superficially attractive, populist options, such as unilaterally restructuring debt, imposing new payments restrictions, increasing government intervention in markets, or trying to stimulate expansion by printing money. We know too much,

alas, where such a retrograde approach leads: it would reverse years of progress toward more open economic management, and will quickly undermine countries' capacity to reap the benefits of the global economy.

This being said, it is quite remarkable to see how limited is the impact of these so-called "alternatives" or experiences. The growing majority of countries is striving in the opposite direction, to implement more promising programs based on sound money, budget discipline, state restraint in its economic intervention, structural adjustment, strengthening of financial systems, and promotion of good corporate and public sector governance, in a context of orderly integration in the world economy. These are the only programs we, of course, support. You will be interested to know that more than 80 countries at this very moment are implementing such programs or negotiating them actively with us. These are emerging countries, transition countries, and countries among the poorest, particularly in Africa. Let's salute their courage and wisdom.

* * *

As you can see, we are far from being a moribund institution, preoccupied with questions about our future. What concerns us is the future of the international monetary system. And this is why, while being so busy with our work as a fire brigade for the world economy, we are devoting attention to detailed reflection on the global or systemic issues that allowed crisis to develop. Thus, looking to the longer term, we have been working with our member governments on proposals to strengthen the architecture of the international financial system, identifying steps that can be taken to minimize the risks of further such crises in the future. This work aims to create a global system that is stable, sound, open, transparent, and fair. This is a tall order. We are working intensely, within the IMF itself, and with other international forums and member governments, to make these ideas operative as soon as possible.

The agenda, a complex one indeed, brings together roles, rights, and obligations for the different constituents of the global economy: governments, citizens, private corporations, and international organizations. Let me give you a snapshot of the work that is in progress at present:

- Strengthening the IMF's surveillance of its members' policies, especially with respect to financial sector issues and capital flows;
- Improving the soundness of financial systems through widespread adoption of consistent standards and practices for regulating and supervising banking systems, securities markets, and other financial institutions;
- Strengthening the financial infrastructure through more uniform standards for auditing, accounting, bankruptcy procedures, and payments systems;
- Making the golden rule of transparency prevail, by providing for timely and accurate information in the form of both data and more open communication to the markets about economic policy formulation and results;
- Defining the principles of good governance in both the public and private sectors;
- Continuing firm but orderly progress with freeing capital flows, recognizing that it is a long-term goal for many countries, to be set in the context of properly sequenced financial reform and of a strengthening of macroeconomic balances. As you know, this is a domain for which we received a very clear mandate in Hong Kong to go for freedom and orderly dismantling of capital controls. If anything, contrary to the confusion that seems to have emerged lately, the present crisis encourages us to persevere in this direction;
- Developing ways of involving the private sector in forestalling financial crises and in resolving them if they do occur—a domain, I hope, where the private sector will volunteer suggestions, and in which they will not hesitate, if needed, to take action even before more formal or far-reaching arrangements are put in place;
- And, the bottom line, promoting a permanent dialogue with governments, aiming to ensure that economic and social policies contribute to improve opportunities for all citizens to participate in and benefit from economic progress. This is the ultimate aim of all our efforts.

Even as the architecture is being reinforced, one urgent task needs attention to enable us to continue with our work: it is a question of resources. The IMF's tasks are, simply stated, to offer policy

advice to all members, and to provide financial support to those members that need it and are prepared to make the necessary policy changes. It is evident that with increased global market turbulence, the Fund needs to be able to remain an effective partner with its members as they confront these challenges. This has a name: it is the increase of our quotas—namely our capital base—a decision involving our 182 members. It is still pending, particularly in the United States. I have no doubt that this decision will be taken promptly, as has always been the case in our history, so enabling the Fund not to save the world—this is not its mission—but to help effectively those who strive to save themselves.

* * *

Mr. Chairman, these remarks have been too long. Let me hope that they may be of some help for this attentive audience in evaluating what this crisis is all about, what is the right track toward recovery, and what kind of new financial architecture we should put in place, so as to hit the ground running as we emerge from this crisis.

Toward a New Financial Architecture for a Globalized World

The Group of Seven/Group of Eight Summit will be held in Birmingham next week. High on the Summit agenda will be the issue of how to renovate the architecture of the international financial system in the face of the tremendous changes under way in the global economy. The Asian crisis has been so unexpected in many of its aspects, so broad, so cruel in its human consequences that—even before the crisis has run its full course—the leaders of the world want to embark on the design of a new architecture. This is certainly the right thing to do, and the venue of this meeting could hardly be more fitting. Like many other cities in advanced countries, Birmingham has experienced the forces of change in the global economy firsthand—from the loss of traditional industries to the challenge of finding new employment opportunities. Moreover, two centuries ago, this city was at the heart of the Industrial Revolution, an era that, like our own, was a time of extremely rapid change. At that time, intellectuals of all schools of thought used to meet frequently in Birmingham—every full moon, I understand—and bring their reflections to bear on the challenges of their new world. This was the so-called Lunar Society, which included such personalities as Matthew Boulton, James Watt, Erasmus Darwin (grandfather of Charles), and William Small—a friend of Benjamin Franklin and Thomas Jefferson, all with wide-ranging interests, all sharing a sense of optimism and responsibility for building a better world. Imagine what a blessing it would be if the G-7/G-8—our new Birmingham group—were to be inspired by such an example when dealing with their pressing agenda!

As a modest preface to their work, I would like to share with you my personal views on the need for change the Asian crisis reveals, the building blocks available for a new architecture, and the work already under way at the IMF and, in the best traditions of

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Address at the Royal Institute of International Affairs, London, May 8, 1998.

Chatham House, to fly a few kites and suggest some further steps for the longer term.

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Change Is Needed

As in the days of the Industrial Revolution, we are now at a defining moment of human history. The question before us is straightforward: how to utilize the full potential of globalization to improve the living standards of all—particularly the poorest—while containing the risks it entails, such as those we have seen materialize so brutally in Asia, and those at least equally pernicious, even if less spectacular, of the continuous marginalization of the poorest countries. What kind of new architecture of the global system could achieve this? The response must be deduced from a proper analysis of the most recent crises.

Contrary to what we saw during the debt crisis of the 1980s, the problems in Asia were not almost exclusively macroeconomic in nature; even if these countries suffered, all of them, from some deficiencies in this respect, by and large they had long track records of successful economic management. Rather, in a context dramatically changed by a major realignment between the dollar and the yen, and important differences in short-term yields, three other factors helped trigger the crisis:

- the weakness of their public and private banking and financial structures;
- an unsustainable accumulation of short-term financing—particularly of interbank lending, which Alan Greenspan refers to as the Achilles' heel of the international financial system—which made countries particularly vulnerable to a sudden shift in market sentiment;
- and, last but not least, deep-seated problems of governance, corruption, and what U.S. commentators call "crony capitalism."

Together with the macroeconomic problems, these three major factors had to be addressed for our response to the crisis to be pertinent. If you examine our programs with Thailand, Korea, and Indonesia, you will see that we have tried to deal with these factors, and they will have to be taken into consideration in the future in

whatever efforts are undertaken to avoid the recurrence of crises. But even that will not suffice. In view of the enormous human and economic cost of the Asian crisis, no wonder we hear many radical suggestions as to how to avoid such losses in the future. There are calls for us to do a better job of predicting and preventing crises, addressing their social impact more effectively, stopping speculators and properly regulating this "casino economy," seeing to it that investors bear the full costs of their mistakes, stabilizing the international monetary system, providing for more political accountability of our institution, etc., etc.

We cannot deny the basic justification of these—at times vociferous—calls for change. No doubt there are at least some elements of validity in each of them. Taken together they tell us that, at this stage, world public opinion expects its leaders to design and build a new, common house with an audaciously modern architecture, and not limit themselves to some plumbing and interior decorating of the old mansion.

But, as responsible architects, let us start by recognizing the building blocks at hand. Indeed, they are substantial.

Seven Building Blocks

The first of these building blocks is the tremendous potential for growth and prosperity globalization provides countries fully integrating into the global economy. Formidable sources of dynamism are there, engendered by new information technologies and unifying financial markets. The question, then, is how to discipline and channel these forces so that growth will be sustainable and more broadly shared and the fundamental desire for greater equity will be more fully satisfied.

The second building block is integration. By integrating themselves into the mainstream of the globalizing world economy, the poorest countries will avail themselves of a most powerful instrument of acceleration of development, while, if they preferred to do it alone, they would expose themselves to the risks of marginalization, abandoning several generations to economic stagnation and poverty.

The third building block is the universal consensus on the importance of an increasingly open and liberal system of capital flows in order for globalization to deliver on its promises.

The fourth building block is what we could call the "golden rule" of transparency, now truly seen as the key for modern management, economic success, and rational behavior of global markets.

The fifth is good governance, which is equally essential for strong economies and properly functioning democracies. No doubt, competing for excellence in governance is the modern face of statesmanlike responsibility.

The sixth building block could be a set of standards and codes of best practices; this could require a few words of elaboration. More and more we observe an emerging recognition that the global markets still suffer from the kind of anarchy that afflicted our domestic financial markets here in Europe during the nineteenth and the beginning of the twentieth centuries—that is, until various scandals and crises led to the creation of such institutions and rules as securities and exchange commissions, banking supervision, accounting standards, disclosure and prudential rules, and so forth. Our challenge today is to disseminate these good practices in emerging markets and to establish similar checks and balances in global markets. This could appear an impossible task, as many will pretend that the absence of rules or regulations of any kind has been at the very origin of the developments of these markets. The world community is now coming to a different view, and looks forward for the definition of international standards and codes of good practices, which would be progressively disseminated by the IMF through its surveillance, and could help limit the excesses of an international "casino economy."

Last, but not least, the seventh building block is the option for the multilateral approach to handle problems that are now more and more global in nature. And the key instruments of such an approach will have to be the Bretton Woods institutions themselves. Let me be immodest for a moment. The experience they have accumulated, the quality of their staff, and their demonstrated ability to address new economic challenges promptly and efficiently make them a major asset of the world community and a central pillar of a new architecture, provided they continue adapting themselves, reforming themselves, to this new world. And suggestions for self-reform are in abundant supply.

These seven building blocks have been neglected or unevenly utilized for too long. Assembled in the right way, they could offer a

rock-solid foundation for a new financial system. Assembling them, nevertheless, will be hard work, each of them implying that vested interests or perverse practices be challenged. Thus, notwithstanding our sense of urgency, we are heading here for an evolutionary change: Athena in her helmet will not spring full-grown from the head of Zeus! And, as with all transitions from one era to another, we can expect risks and uncertainties to persist for some years to come. This makes it all the more urgent to get to work on this new architecture right away.

Initial Steps for a New Architecture

In fact, a number of significant steps are already under way. At its April meeting, our governing body, the Interim Committee (of Ministers and Central Bank Governors of IMF member countries), set the broad agenda for the IMF's own work—and its work with others—for the near future. Five areas have been given priority by member governments:

- The central role to be played by the IMF in crisis prevention through its surveillance and its role in encouraging members to strengthen their macroeconomic policies and financial sectors.[1]

  The Interim Committee suggests that the Fund intensify its work in surveillance of financial sector issues and capital flows, and focus on the risks posed by potentially abrupt reversals of capital flows, especially those of a short-term nature. The Fund is also asked to examine ways to strengthen

[1]Of course, it is clear that for IMF surveillance to be effective, member countries must provide timely, accurate, and comprehensive data to the Fund. The Interim Committee underscored members' obligation in this regard and suggested delaying the Fund's reviews of member economies when deficiencies in disclosing relevant information to the IMF seriously impede our surveillance. Indeed, the G-7 countries have the opportunity this week to establish leadership by pledging to convey to the IMF and to publish comprehensive and timely data on both gross and net reserves, including reserve-related liabilities and central bank derivative transactions and positions, as well as external debt and data on banking and financial sector health.

the monitoring of capital flows, a major and difficult undertaking indeed!

- Drawing on the lessons from the Asian crisis, and the frustration that confidential warnings from the Fund were not always heeded, the Fund has been asked to develop a "tiered response," whereby countries that are believed to be seriously off course in their policies are given increasingly strong warnings. Addressing an audience in this country, where football is a way of life, or in my own country in advance of the World Cup, I do not need to emphasize how important it is to know exactly when the referee has shown a yellow card and how many yellow cards are permitted! We also have the red card in our Articles of Agreement, but using this card could precipitate the crisis we seek to avoid. So we prefer to use the yellow card.
- The Interim Committee also called upon the IMF to help members strengthen their domestic financial systems by encouraging them to develop supervisory and regulatory frameworks that are consistent with internationally accepted best practices, as well as strengthened standards for bank and nonbank institutions. Here you will recognize, of course, the "standards and good practices" building block. Work in this area is already in progress in various forums. A notable example is the Basle Committee's Core Principles for strengthening banking regulation and supervision, which the IMF is now helping to disseminate to member countries. We will now work with other relevant institutions that could be responsible for developing similar standards in areas such as accounting, auditing, disclosure, asset valuation, bankruptcy, and corporate governance. We will also consider how to disseminate such standards to member countries through our surveillance and encourage their adoption. Working with so many institutions, public and private, in addition to our 182 member countries, will be an ambitious undertaking, but we are ready—and enthusiastic—to play our full part in this new chapter in international cooperation.

In the meantime, the IMF has been applying this "standards" approach to one of its traditional domains of expertise: fiscal policy. Last winter, following the suggestion of the Chancellor of

Exchequer, the IMF developed a code of good practices on fiscal transparency to which members will be encouraged to adhere. Looking ahead, we plan to develop a similar code with respect to financial and monetary policies in cooperation with the appropriate institutions.

- But despite these efforts at crisis prevention, crises may continue to arise from time to time. In this regard, the Interim Committee also reaffirmed both the central role of the Fund in crisis management and the need to develop more effective procedures to involve the private sector in forestalling or resolving financial crises.[2]
- Finally, as I have already alluded, the Committee reaffirmed its view that the time has come to add a new chapter to the Bretton Woods agreement by making the liberalization of capital movements one of the purposes of the Fund and extending, as needed, the Fund's jurisdiction for this purpose. It requested the Executive Board to pursue its work on this issue with determination, with the aim of submitting an appropriate amendment of our Articles of Agreement as soon as possible.

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[2]As regards the latter, some follow-up actions are needed, including measures to discourage excessive reliance on short-term financing and strengthen countries' capacity to withstand sudden shifts in market sentiment. In addition, the Interim Committee has requested the Fund to consider other ways to strengthen incentives for creditors to use available information to analyze risks appropriately and avoid excessive risk taking. Possibilities include introducing provisions in bond contracts regarding bondholder representation and voting in case of negotiations on bond restructuring; extending the Fund's policy of providing financing to member countries in arrears to private creditors; encouraging strong bankruptcy systems for both domestic and international capital markets; and advising member countries to exercise greater caution in granting public guarantees. We also need to examine the possibility of closer contacts with creditors in order to explain Fund arrangements and, if needed, catalyze private sector financing so as to achieve more equitable burden sharing vis-à-vis the official sector and limit moral hazard.

Establishing closer contacts with private creditors, particularly at an early stage of a crisis, raises difficult issues; thus, it is not surprising that the Interim Committee has not pronounced on this point. Among the various options, I would suggest that consideration be given to asking the appropriate authorities in each creditor country to arrange for the selection of a representative of its financial community, who could be contacted in a crisis and who could provide a channel for communicating with a wide spectrum of financial institutions.

Greater transparency and availability of economic information, adoption of standards and dissemination of best practices, a continuous strengthening of IMF surveillance, the orderly liberalization of capital movements, and better private sector involvement in crisis prevention and resolution—taken together and utilized to their full potential, these first five pillars could be a very significant contribution to a new financial architecture much more attune to dramatically modernized and globalized markets. I have no doubt the G-7/G-8 leaders in Birmingham will invite us to build on this basis. One can even imagine that they want to point out some additional avenues, which, as we have been absorbed by more immediately pressing aspects of our work—we have not, as yet, been able to explore sufficiently.

What Next?

Trying to answer the question of "what next" is a risky endeavor. No doubt with globalization unfolding its opportunities and risks, new priorities will promptly capture our attention and overtake our pre-established agendas. But it is always better to try to anticipate them, particularly when they reflect problems that should already have been addressed, be it:

- the integration of the poorest countries in the globalized economy (Asia should not distract us from the pressing problems of the poorest economies);
- the stabilization of the international monetary system; or
- the issue of the democratic accountability of international financial institutions, as far as the IMF is concerned.

The issue of the integration of the poorest countries is, of course, already on our agenda. But, true, the attention of the world has been so focused on the Asian crisis and the need to avoid its recurrence that the immense problem of development and alleviation of poverty, particularly in Africa, seems to have been put temporarily on a back burner. This is no longer acceptable.

In this context, I was particularly happy that, in drawing the lessons of an external evaluation of the Enhanced Structural Adjustment Facility (ESAF), the Interim Committee encouraged us to "strengthen the ability of the Fund to foster sustained growth and external viability in poor countries." There is more than conventional

rhetoric in these words. This mention, in a document essentially devoted to the handling of financial crisis, surely testifies to the recognition by the world's financial leaders that the success or failure of poor countries in finding their own way toward integration and development in an interdependent world will have a major influence on what the twenty-first century will be. This means that the solidity of our new architecture will crucially depend on the way in which, for the poorest countries, monetary and financial strategies, on the one hand, and poverty alleviation strategies, on the other hand, are made mutually reinforcing.

Poverty alleviation is chiefly, of course, the task of the World Bank, the regional development banks, and bilateral donors. Among the latter, it is quite encouraging, indeed, to see the energy and enthusiasm with which the British Minister for Development—an MP from Birmingham, as a matter of fact!—Ms. Clare Short, is promoting the Development Assistance Committee Target of reducing by one-half the proportion of the world's population living in extreme poverty by 2015.[3] These objectives are ambitious, but they remain realistic, provided industrial countries join forces in stopping the present decline of development assistance and implement their agreed commitment to support, as needed, countries that truly own their national strategies for sustainable development. Among the latter, I would agree that particular priority be given to postconflict countries where we must join forces to give new chances to reconciliation, peace, and development. Obeying this same imperative of serving together peace and development, I would also suggest that the G-7/G-8 warmly endorse Mr. Koffi Annan's recommendation to the African governments to reduce purchases of arms and munitions to 1½ percent of GDP and maintain zero growth on defense budgets for the next decade. Industrial countries must play their full part in these efforts, and, here, I must share with you my anxiety.

Today's silence on the crisis in official development assistance is profound and distressing. It means that Africa, in particular, must rely chiefly for its economic progress on humanitarian compassion or the benefits of trade. This cannot suffice if human development is to be intensified and accelerated. Yet, at the present juncture, the

[3]I hope I am not revealing a state secret in telling you that she inscribed this on her Christmas card!

macroeconomic and structural successes of recent years, precisely in the context of IMF–World Bank supported programs, are creating an opportunity that is too good to miss. Africa has found a way to advance from two decades of negative per capita growth to positive growth in more than 40 of its countries. In many African countries, a new generation of leaders is seriously concerned about the need for democratization, protection of human rights, promotion of "good governance," and human development. Their efforts are in danger of falling short, however, because their domestic savings rates are still too low to finance the volume of investments needed to boost their rate of growth from approximately 5 percent to over 7 percent, which is not an unrealistic objective; it could be attained and sustained for a long time if local savings were supplemented by an appropriate mix of public and private foreign support and if a few key conditions were met, notably:

- continued modernization of the framework for private investment; and
- improvement in public governance through the total commitment of new governing teams.

Together with the World Bank and bilateral donors, we can make a difference. But a strong political impulsion by the world's leaders and the example of their countries' cooperation to development will be of the essence. May their communiqué demonstrate their vision and leadership in this domain also.

The stability of the international monetary system has been on the agenda for more than 20 years of annual summits. The Asian crisis has highlighted how disruptive developments in exchange markets can help trigger a crisis. It is in this domain that efforts to strengthen multilateral surveillance over the international monetary system could be particularly fruitful. Moreover, the development of the euro into a key international currency could make a major contribution to the stability of the overall architecture, provided that close cooperation is established among the monetary authorities of the tripolar system that might take shape. Even if it would be premature at this stage to try to elaborate further on how to maximize the positive effects of this major innovation, no doubt the new international monetary equilibrium will have to be kept under review as a key element of the new architecture. From the outset, effective means of coordination will have to be found to avoid excessive mis-

alignments and disruptive corrections. The world is fully justified in expecting a responsible leadership from these major currency blocs, which should be actively mindful of their global responsibility and resist the temptation of "benign neglect."

Lastly, at a time when de facto more and more responsibilities are being given to the international financial institutions, and particularly to the IMF, the question of their political accountability will probably be raised with increasing insistence. Indeed, this question already arises from time to time, although not always with full awareness of the nature of our institutions and of the powerful checks and balances already enshrined in their Articles of Agreement. In this context, and as far as the IMF is concerned, is there anything that could be done to strengthen what one might call the political accountability or legitimacy of our institutions? At this stage, this would require at least a few organizational changes, which would make more explicit the tie that binds us to the governments we depend on. The IMF could, for instance, encourage its Governors, in general the Ministers of Finance, to become more actively involved in its work, in terms of decision making and not merely in a consultative capacity in the Interim Committee. A similar question faces the G-7, which feels the need to embrace emerging market countries, but is unclear about how to go about it, and finds it difficult to come up with acceptable ways of choosing its partners. The design of a new architecture provides, perhaps, a good occasion to address these long-avoided questions. Two avenues could be explored.

The first would be to "revitalize" the IMF Interim Committee. It could become an essential structure, because no other can match the scope of its responsibility and the legitimacy of its members, who are collectively responsible for key developments in the world economy. At present, however, it is hampered by the ritualism of its meetings and an insufficient awareness of its uniqueness and potential. This is why I think that the suggestion of the French Minister of Finance, M. Strauss-Kahn, to consider its transformation into a "Council" with decision-making, rather than merely consultative, powers, is particularly important. This is not a new idea. This transformation, pursuant to Article XII, Section 1 of the Fund's Articles of Agreement, could give it a new start. This approach was envisaged under the Jamaica accords, but deferred at the time because of

the experimental nature of the Interim Committee. But given the daunting changes that have occurred recently in the world economy, and the fact that the IMF has achieved truly universal status with the accession of the transition countries, perhaps the time has come to consider it. Without greatly altering the operation of the institution and the pivotal role of its Executive Board, such a transformation would give the IMF renewed and very valuable legitimacy for the increasingly difficult tasks it is called upon to perform.[4]

The second avenue, in the same spirit, would consist of making provisions every two years for the G-7/G-8—on the occasion of their meetings—to join the heads of state and government of the 16 countries holding seats on the IMF and World Bank Executive Boards to discuss with them and with the heads of those two institutions and the World Trade Organization the major economic and financial questions of the day. This new Group of Twenty-Four would have the significant merit of its basic legitimacy, as it would strictly reflect the system of international representation established for monetary and financial affairs in Bretton Woods. This would clearly represent a step forward not only in terms of dispelling the current malaise, but also in terms of hastening the adoption of integrated policy responses to the challenges of the globalized economy. The Secretary-General of the United Nations should also be invited to participate to take into account the work of the entire family of UN agencies, which could become a fourth humanitarian and social pillar of the world system.

Such ideas could, of course, be met with skepticism and run up against logistical problems that may seem insurmountable. Nevertheless, they need to be discussed, as they could provide a concrete way of recognizing that each medium-sized or developing country must have a more equitable share of responsibility for the future of the world economy, a share that they believe is unjustly denied them in the present institutional arrangements of the international financial system.

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[4]This decision must be taken by an 85 percent majority and thus requires the active support of all G-7 members.

Now, at the end of this analysis of a number of key issues confronting the world economy, it is perhaps appropriate to come back for one minute to the central messages of our eminent predecessors of the Lunar Society two hundred years ago. I am told that they included:

- the value of drawing lessons and inspiration from various disciplines and from the experience in different countries;
- the need to establish and disseminate standards so quality would be upheld and trade would flourish;
- a deep concern for the social implications of economic change and a keen desire to improve education;
- and, of course, a strong sense of purpose and confidence in the promises of their new world.

No doubt these messages could strike a chord with many people today, including—why not?—the stellar group that will assemble in Birmingham. May they share these approaches and concerns. Their confidence in the lasting benefits of globalization will be fully justified as a new world, born from the opening of economies, the unification of markets, and the universal availability of information and knowledge, has an immense potential for high-quality growth. May they also validate their own message of confidence by a clear demonstration of their sense of universal responsibility and solidarity.

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The IMF and Good Governance

Ladies and gentlemen, I am very pleased to participate in this forum, not only because of the importance of transparency and good governance, but also because it gives me the opportunity to express my admiration for the work that Transparency International is doing around the world. By helping to enhance public sector accountability and transparency and developing greater public awareness about the need for and requirements of good governance, your organization is performing a vital service to individual countries and the global economy. So I was very pleased in looking at my schedule following the most recent series of negotiations in Asia to find an opening—all too small, but large enough—for me to come to pay tribute to the work that you do. On the advice of my friend and former colleague at the Ministry of Finance, Mr. Dommel, I will do so by describing the IMF's activities in this field and recounting, without embellishment, our experience in Asia.

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The IMF's role in governance issues has been evolving over the years, and good governance has taken on increasing importance in our traditional mandate of promoting economic stability and what I call high-quality growth. It is not only the IMF, but also its member countries that have awakened to this concern, although with varying degrees of enthusiasm. Indeed, as recently as a few years ago, there was little support among our members for the IMF, or for any other international financial institution, to become more actively involved in governance issues. Some of our shareholders feared that in taking on such issues the institutions would become politicized and lose their effectiveness—don't we have enough to do in our missions to preserve monetary and exchange stability? Others attached higher priority to other issues. In short, there was no shortage of excuses for keeping us at arm's length. Today, however, not only have gover-

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Address at Transparency International (France), Paris, January 21, 1998.

nance issues moved to the forefront of discussion, but in many cases government reform has moved to the top of the policy agenda. What has changed?

One important change has been in the perception of what constitutes sound economic policy. As more and more evidence has come to light about the adverse consequences of governance problems on economic performance—among them, losses in government revenue, lower-quality public investment and public services, reduced private investment, and the loss of public confidence in government—a broader consensus has emerged on the central importance of transparency and good governance in achieving economic success.

Numerous studies have shown that where governance is poor, domestic investment and growth suffer.[1] Moreover, in a world in which private capital has become more mobile, there is mounting evidence that corruption undermines the confidence of the most serious investors and adversely affects private capital inflows—this is the case in all too many countries in Africa. Even Asia is no exception; we have seen there that governance problems can also undermine the ability of countries to channel private capital inflows into productive, long-term investment. Moreover, the Asian crisis has demonstrated in a very dramatic way how the lack of transparency about underlying economic and financial conditions can feed market uncertainty and trigger large capital outflows that can, in turn, threaten macroeconomic stability. Conversely, progress toward greater transparency can radically alter the very terms of the public debate.

Other factors also come into play. With government budgets under pressure in virtually every country in the world, bilateral aid donors have become more conscious of the need to direct their resources to countries that they believe will use those resources most productively and in which such use can be monitored. The IMF itself has a responsibility to its members to ensure that the resources they provide to the Fund are put to good use.

For all of these reasons, our member countries have come to recognize the vital importance of good governance, and, at our Annual Meetings in September 1996, a *Declaration on Partnership*

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[1]See, for example, Mauro, Paulo, 1997, *Why Worry About Corruption?* Economic Issue No. 6 (Washington: International Monetary Fund).

for Sustainable Growth was adopted, though, paradoxically, despite its fundamental importance it appears to have gone unnoticed. It reflects a now universal consensus on these issues, and states that "promoting good governance in all its aspects, including ensuring the rule of law, improving the efficiency and accountability of the public sector, and tackling corruption" is an essential element of an environment in which countries can achieve lasting prosperity. It may seem like a catchall, but its words give legitimacy to our efforts in this area and to the "second generation of reform" that we are now trying to promote. Subsequently, the IMF's Executive Board met a number of times to develop guidance for our staff in dealing with governance issues. The result was a set of guidelines that have been in effect since last July.[2] They confirm and strengthen the approach that the Fund has been taking for some time, and also stress the importance of addressing governance issues evenhandedly in all member countries and, of course, the need to work together on these issues with other multilateral institutions, especially the World Bank, since we are jointly confronted with these problems.

So how does the IMF go about promoting good governance? Not by systematically seeking out all cases of corruption in the world, but by helping members improve the management of their public resources and establish a stable and transparent regulatory environment for private sector activity, a *sine qua non* for economic efficiency and the eradication of corruption.

Broadly speaking, our approach is to maximize the transparency of government financial operations and create systems that minimize the scope for making decisions on an ad hoc basis and for giving preferential treatment to individuals and organizations. For example, we are helping members simplify their tax systems and business legislation and strengthen tax and customs administration by eliminating special exemptions that apply to a privileged few; this is the best means of ensuring that adequate revenues are received to finance essential public services and that such services are accessible to the general population. Likewise, we are working with countries to strengthen and increase the transparency of budgetary procedures to ensure that government revenues are fully accounted for and used

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[2]*Good Governance: The IMF's Role* (Washington: International Monetary Fund, August 1997).

as agreed in the budget. We are also seeking to improve the quality of government expenditure by reducing outlays for unproductive purposes, such as costly military buildups and large projects that benefit influential groups while stroking the egos of the high and mighty. The savings will make room for spending on primary health care, basic education, vocational training, and essential infrastructure.

At the same time, the IMF seeks to promote more effective and accountable economic and financial institutions. To this end we are working to improve the quality of financial sector regulation and supervision and enhance the transparency of financial sector operations. Similarly, we are encouraging countries to improve the quality of the data they provide to the public about domestic economic and financial policies and performance. We cannot overemphasize the importance of high-quality statistical data; such data are an influential factor in improving economy policy and an essential aid to potential investors in evaluating countries' economic policies and performance. They allow the markets to become more informed and selective, and constitute a first-class protection for countries with good policies, which will be less vulnerable to the often capricious fluctuations and herd behavior on the financial markets. Certainly, these examples will not come as any surprise to you. In fact, you have probably noticed the similarity between the measures that the IMF is advocating and the areas of reform that the Transparency International Source Book has identified as useful elements of an overall anticorruption strategy.

Corruption. What specifically are we doing to combat corruption? Our institution has a macroeconomic mission, and our mandate is restricted to those specific instances of corruption that may have a significant—some would say demonstrable—macroeconomic impact. We do not hesitate to bring such cases to the attention of the authorities. The macroeconomic nature of corruption may be identified by the large amounts involved or the fear that specific cases of corruption are symptomatic of a wider governance problem. Examples might include tax and customs fraud with the involvement of senior public officials, the misuse of official foreign exchange reserves, and abuses of power by bank supervisors or failure on their part to take action. This has led us in some cases to delay or suspend our support until the member in question has taken appropriate corrective action, such as presenting external audit reports, canceling illegal contracts,

and removing or even taking legal action against key officials found to be at the center of fraudulent practices.

Need I add that, in our view, good governance is essential for countries at all stages of development—from the poorest countries that are still in the process of building up domestic institutions and undertaking the basic reforms needed to accelerate economic growth to the advanced countries, both as regards their own internal governance and their dealings with developing countries. In this connection, I welcome the commitment of OECD countries to criminalize the bribery of foreign officials and put an end to the tax deductibility of these so-called fees, which are really nothing more than bribes. But let me move from the theoretical to the factual and focus briefly on an experience that is still very much on my mind: the current problems in Asia. I am especially eager to tackle this subject as it is the first time in the history of the IMF that we are applying, on a very large scale I might add, the new mandate that we have been given in this field.

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In recent months, the world has been shocked to see how quickly countries renowned for outstanding economic performance have been engulfed in crisis. Although the causes of the crisis are varied and complex, many of the problems that lie at the heart of Asia's difficulties are bound up with poor governance. In Korea, for example, opacity had become systemic, as in the case of the chaebols, which are to be completely overhauled under the negotiated program. In addition, relationships among governments, corporations, and financial institutions were so close—I have even gone so far as to say incestuous—that in the long run they could only result in unclear accountability and disastrous investment and lending decisions, ultimately undermining banking sector health and impeding competition. Finally, the lack of transparency about government, corporate, and financial sector operations concealed the extent of Korea's problems, so much so that corrective action came too late and ultimately could not prevent the collapse of market confidence, with the IMF finally being authorized to intervene just days before potential bankruptcy.

The situations in Thailand and Indonesia have forced us to deal with similar problems, although to a lesser or different degree. Our

programs in these three countries have been designed to go to the heart of these problems. In each case, the centerpiece of the program is a thorough restructuring of the financial sector. The goal is to ensure that owners and managers are genuinely more accountable for the prudent operation of their banks, that loans are made on the basis of objective commercial criteria, and that banks return to their essential role of mobilizing domestic savings and promoting sound investment. We must make sure that insolvent institutions are closed down, and that their owners and managers share in the losses. We are also calling for institutions that are simply illiquid to come up with restructuring plans that bring them into compliance, within a relatively short time and in full transparency, with internationally accepted accounting practices and disclosure rules, and with the Basle capital adequacy standards. Also required are institutional changes to strengthen financial sector regulation and supervision.

The programs are no less ambitious as regards the corporate sector. They include measures to improve the transparency of corporate balance sheets through independent external audits, disclosure, and publication of consolidated statements for business conglomerates so that markets can monitor corporate performance. At the same time, the programs seek to create a more level playing field for private sector activity by dismantling monopolies, eliminating government-directed lending, increasing the transparency of foreign trade procedures, and revising government procurement and contracting regulations. Bankruptcy laws are to be allowed to work without government interference. Meanwhile, the opening of domestic markets to foreign participants should help stimulate domestic competition and encourage domestic firms to adjust. The media have discussed the scope and coverage of the Indonesian program at length, so I won't go into further detail about the arm wrestling we had to do with the directors of monopolies and cartels of all kinds.

Just as corporations and financial institutions must become more open and transparent, so too must their governments. All three programs call for governments to improve the publication of key economic data and bring off-budget activities into the budget so as to provide a clearer picture of the financial position of the wider public sector and improve its governance. The programs are far-reaching; the Indonesian Fund for Reforestation is just one example.

Yes, the programs are far-reaching and confirm the basic intuition of your organization: that anyone who takes the need for transparency seriously will profoundly change the course of events. If you permit me to paraphrase the words of the Duc de Liancourt, Master of the Robes to Louis XVI, on July 14, 1789, I would say: "It's not progress, Sire, it's a revolution!" Such reforms will require a vast change in domestic business practices, corporate culture, and government behavior. Obviously, this will be a long-term process—a process in which the IMF, the World Bank, and others can assist, but one whose success depends on the efforts of the countries themselves. However, the positive effects are already being felt: witness the attitude of the Korean unions. They were convinced to give up the idea of a general strike in return for a tripartite dialogue with the government and employers regarding the accounts of the chaebols, which are finally more transparent and more widely disseminated. I think we will have turned the corner in the current crisis when markets become fully aware of these changes. In any event, it is heartening to see the determination with which President-elect Kim Dae-Jung appears set to address these issues in Korea. I hope other country authorities will follow his example.

"Revolution!" It is probably too strong a word. History will judge, but for the IMF, which for 50 years confined itself essentially, in accordance with its mandate and not without some success, to helping its member countries accept essential monetary and macroeconomic discipline, these are entirely new frontiers, both vast and promising, as they are for the World Bank and the other major international organizations. However, we must guard against leaving this work to the international organizations, which risks setting them up as the scapegoat for all the world's ills if progress should come too slowly. Like all revolutions, this one will be successful only with the unrelenting and ultimately irresistible pressure of civil society. Spearheading this effort, Transparency International has already contributed to bringing about change. The IMF is proud to work alongside Transparency International in this vitally important effort: on it depend good governance in service of society and the opportunity for a new form of citizenship.

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Rebuilding Confidence in Asia

Thank you, ladies and gentlemen. I am very pleased to have this opportunity to speak to you, the business leaders of Southeast Asia, at this critical moment in the region's economy. The crisis that began in Thailand has now shaken a number of other economies in the region, and its aftershocks have been felt as far away as Latin America and eastern Europe. Countries that have been accustomed to, in some cases, decades of high growth now face the prospect of a marked slowdown in economic activity. This has prompted some observers to suggest that perhaps the so-called Asian miracle was only a "mirage."

I do not hold that view. In my opinion, the region's economic success over the last couple of decades can be described in many ways—as outstanding, superlative, and certainly admirable. But it was no "miracle." Rather, it was the result of good policies that fostered saving and investment, including in human development; encouraged innovation and entrepreneurship and a quick response to market signals; and promoted trade. Recent developments have not wiped out past achievements. On the contrary, the region's longer term fundamentals—including its high domestic savings rates, strong fiscal positions, dynamic private sectors, and competitiveness—remain favorable. Moreover, most Asian countries still have a long way to go to catch up with advanced economies. Thus, to all the prophets of gloom and doom I would reply that with a lucid diagnosis of the problems, without complacency, and with appropriate economic adjustments now and sound policies in the future, these countries will be able to rekindle—in a more sustainable way—high rates of growth in the coming years.

In a situation, like the current one, that is evolving quickly, it is difficult to step back and take a longer view. But indeed that is what is required to get to the root of the region's problems and find appropriate solutions. In this spirit, I would like to talk very candidly with

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Remarks at the Association of South East Asian Nations (ASEAN) Business Forum, Kuala Lumpur, Malaysia, December 2, 1997.

you about the causes of the current crisis and what they suggest about the requirements for rebuilding confidence in this dynamic region.

Causes of the Crisis

Let me start with the question that so many have asked: how could events in Southeast Asia unfold this way, after so many years of outstanding economic performance?

In the case of Thailand, the answer is fairly clear. To begin with, standard economic indicators revealed large macroeconomic imbalances: the real exchange rate had appreciated considerably; export growth had slowed markedly; the current account deficit was persistently large and was financed increasingly by short-term inflows; and external debt was rising quickly. These problems, in turn, exposed other weaknesses in the economy, including substantial, unhedged foreign borrowing by the private sector, an inflated property market, and a weak and overexposed banking system.

Markets pointed to the unsustainability of Thailand's policies: equity prices declined, and the exchange rate came under increasing pressure. The IMF stressed these problems and pressed for urgent action in a continuous dialogue with the Thai authorities during the 18 months leading up to the floating of the baht last July. But after so many years of outstanding macroeconomic performance, it was difficult for the authorities in Thailand—as in other countries—to recognize that severe underlying problems could seriously jeopardize their track record. And this "denial syndrome" contributed to the delay in taking corrective measures. Finally, in the absence of convincing action, the crisis broke.

We all have been troubled by developments in the Thai economy, both because they have been so costly for Thailand and its neighbors and because they were so preventable. But at least the origins of Thailand's problems are, by and large, clear. The more vexing question is why the crisis spread to other countries, such as Indonesia, Malaysia, the Philippines, and Korea.

Part of the explanation has to do with the fact that developments in the Thai economy undermined conditions in neighboring countries. For example, the depreciation of the baht was expected to erode the competitiveness of Thailand's trading partners, and that, in turn, put pressure on their currencies.

But beyond that, developments in Thailand prompted market participants—especially those who had initially underestimated the problems in Thailand—to take a much closer look at the risks in other countries. And what they saw—to different degrees in different economies—were many of the same problems affecting the Thai economy, including overvalued real estate markets, weak and overextended banking sectors, poor prudential supervision, and substantial private short-term borrowing in foreign currency. Moreover, after Thailand, markets began to look more critically at weaknesses they had previously considered minor, or at least manageable, given time. In other words, markets became less forgiving.

Market doubts were compounded by a general lack of transparency—about the extent of government and central bank liabilities; about the underlying health of the financial sectors; and about the links between banks, industry, and government and their possible impact on economic policy. In the absence of adequate information, markets tended to fear the worst and to doubt the capacity of governments to take timely corrective action. The imposition of controls on market activity—and the threat of future controls—not only made investments riskier, but tended to reinforce the view that governments were addressing the symptoms, rather than the causes, of their problems. This sent investors fleeing to safer havens and set back other efforts to restore confidence.

But perhaps the most important factor in the depreciation of exchange rates was the rush by domestic corporations to buy foreign exchange. Expecting that exchange rates would remain stable indefinitely, and in the context of inefficient banking systems, domestic firms had borrowed heavily in foreign currencies in order to take advantage of lower interest rates available in other markets. Once they recognized that the peg might not hold and that their debt service costs might rise, perhaps dramatically, they hastened to sell domestic currency, extending the currency slide.

Finally, in some cases, the contagion can be traced in part to the "denial syndrome" that I referred to earlier—to the conviction that "it couldn't happen to us."

Questions have also arisen about the role of hedge funds. At the request of the New Arrangements to Borrow (NAB) countries, the IMF has been looking into this question, talking to market participants and central banks about how hedge funds are set up and regu-

lated, and what role they may have played in the crisis. But from what we know so far, it would be a mistake to blame hedge funds or other market participants for the turmoil in Asia. Turbulence in the market is only a symptom of more serious underlying problems, which are now being addressed seriously in many countries. Nevertheless, there are things that can be done to promote a more orderly working of the markets. For instance, consideration could be given to strengthening large trader reporting requirements; limiting position taking by requiring bankers and brokers to raise collateral and margin requirements so as to limit the use of leverage by hedge funds and other large investors; and other efforts to discourage herd behavior and avoid one-way bets, such as providing better information to markets on government policies and the condition of domestic financial institutions, to encourage investors to trade on fundamentals rather than to run with the herd.

* * *

So what does all of this imply about the way in which governments should manage their economies and approach the markets?

The first implication is the most obvious one: the necessity of taking early action to correct macroeconomic imbalances before they precipitate a crisis. This did not happen in Thailand, despite timely and vigorous warnings. Instead, policymakers attacked the symptom of the crisis—the pressure on the baht—and accumulated large reserve losses and forward foreign exchange liabilities in the process. This, together with delays in addressing Thailand's severe financial sector problems and lingering political uncertainties, clearly contributed to a deepening of the crisis and its spread to other economies in the region.

Second, countries may find that they are more vulnerable to crises in other markets than their own economic fundamentals would suggest. Consequently, they may need to take preemptive action to strengthen their policies. Several suggestions come to mind as to where such action might be needed:

- one, maintaining an appropriate exchange rate and exchange rate regime. Clearly, there is no single "right" choice, but more flexible exchange rates can help provide early and visible signals of the need for policy adjustments and are less

likely to invite reckless behavior on the part of borrowers and lenders. But regardless of the exchange rate arrangement chosen, appropriate macroeconomic policies are essential to ensure its success;

- two, maintaining an appropriate macroeconomic policy mix to ensure that fiscal positions do not lead to unduly high domestic interest rates, which, in many cases, have contributed to excessive amounts of short-term capital inflows;
- three, strengthening structural policies—especially the policies and institutions, such as prudential supervision, needed to underpin a sound financial system. In particular, it is important that fragilities in the financial system are not allowed to become so acute that the authorities are unwilling to use the interest rate instrument in times of international financial instability; and
- four, carrying out other supporting reforms—what we call "second generation" reforms—to promote domestic competition, increase transparency and accountability, improve governance, help ensure that the benefits of future growth are widely shared, and otherwise strengthen the foundations for future growth.

Developments have shown that whether a country follows prudent policies is not simply a matter of national concern. As we have seen in this region, spillover and contagion effects can be so rapid and so costly to countries with basically sound policies that every country has a strong interest in seeing that its neighbors manage their economies well. Experience shows that there is considerable scope for improving policies when neighboring countries get together on a regular basis to encourage one another—and, at times, to exert some peer pressure on one another—to pursue sound policies. For this reason, it is very encouraging to see the efforts under way to develop a mechanism for more intensive surveillance and dialogue among participating finance ministries and central banks of the Pacific Rim to complement the IMF's global surveillance over its members' policies and performance. Of course, to be effective, regional surveillance has to be based on sound economic analysis. In this connection, the IMF stands ready to contribute to regional surveillance in Asia, as requested in the recent Manila meeting and Vancouver

Summit meetings, and as it already does in the G-7 and other forums.

Developments in Southeast Asia also offer some insight into how governments should approach markets. Perhaps the best place to start would be by giving credit where credit is due: the capital provided by global markets has been a key factor in Southeast Asia's exceptional growth rates and its ability to lift so many out of poverty. Certainly, there are risks in tapping global markets. But markets also provide tremendous opportunities to accelerate growth and development, as Southeast Asia itself so vividly shows. The key is to approach markets in a responsible manner—with strong macroeconomic fundamentals and sound structural policies that give markets confidence and therefore encourage long-term investment; with respect for the signals that markets provide; and with transparent and market-friendly policies that allow markets to allocate resources efficiently.

Let me say a few more words about the benefits of openness and transparency. When economic policies are transparent, policymakers have more incentive to pursue sound policies. If I may cite one pointed example among many: would the Central Bank of Thailand have accumulated such large forward liabilities if the public had had regular access to information on central bank operations? On the contrary, the authorities would have had to face the problem of Thailand's dwindling reserves much sooner; and most likely, they would have taken corrective action before reserve losses became so large.

Likewise, when timely, accurate, and comprehensive data are readily available, markets adjust more smoothly. Thus, countries are less vulnerable to adverse market reactions when problems eventually come to light, as indeed they always do. Especially when governments are trying to rebuild confidence, a free flow of information allows markets to assess the extent of underlying problems and the seriousness of efforts to correct them. Of course, transparency also limits the opportunities for corruption, which can otherwise distort resource allocation, undermine investor confidence, and inhibit growth. For all of these reasons, openness and transparency can make a substantial contribution to better policies, more stable markets, and hence, more sustainable growth.

Ultimately, the crisis in Asia underlines the need for an orderly liberalization of capital flows to ensure that a greater number of

countries can benefit from access to international capital markets, while reducing risks. This does not mean a return to antiquated methods of capital controls, nor does it mean a mad rush to immediate, full liberalization regardless of the risks. Thus, we are working toward an amendment of our Articles of Agreement to include the liberalization of capital flows as a mandate of the IMF and to broaden the institution's jurisdiction to include capital movements, so as to ensure orderly liberalization and proper sequencing and that other requirements to reduce the risks and maximize the benefits of tapping global markets are in place.

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As developments have shown, confidence, once lost, is hard to regain. Restoring confidence takes a strong commitment to economic adjustment and reform demonstrated by the implementation of what are often painful measures. It also takes openness and transparency. And, of course, it takes time.

That process is now under way in Southeast Asia. The first step has been to design effective strategies to reinforce macroeconomic policies, as needed, strengthen financial systems, and lay the basis for robust growth to resume. With the support of the IMF, Japan, and others in the region, Thailand's new government has recommitted itself to a courageous and comprehensive program that addresses the problems of large external deficits and troubled financial institutions. As a result, the budget is moving back into surplus and a comprehensive restructuring of the financial sector is getting under way. The Philippines has extended its program with the IMF under which a substantial amount of economic adjustment and reform had already taken place. Indonesia has embarked on a major Fund-supported program to strengthen monetary and fiscal policies, restructure the financial sector, and deregulate the economy. South Korea is now working closely with the IMF to design a similar program that we expect will be worthy of broad international support.

Now comes the more difficult task: implementation. This is the task of the national authorities, and it takes leadership. One aspect of this leadership is to take responsibility for the programs being implemented, explain to citizens why adjustment is needed, and enlist their support. Too often citizens have the impression that the pro-

grams their governments are attempting to carry out have been imposed from outside. To authorities who have to carry out painful measures, this may seem convenient; but it is counterproductive because it undermines public support for their efforts. The IMF works very closely with the country authorities to design effective programs. We give our views on the pros and cons of various adjustment measures and on which combinations of measures are likely to work. Needless to say, we do not support programs we think will be ineffective. But ultimately, it is the authorities' decision what the program consists of. Our requirements are: one, that the program be well designed; and two, that it have the authorities' full support.

That being said, the IMF is there to help the countries of this region pull through this difficult period. The staff and management of the IMF are in constant dialogue with the authorities in the region. The programs we are supporting with our financial resources are bold, but realistic, and go to the heart of these economies' problems. In the case of Thailand, Indonesia, and soon Korea, IMF support has helped mobilize additional resources from other bilateral and multilateral resources. Along with the World Bank, the Asian Development Bank, and others, we are also providing a considerable amount of technical assistance, especially on financial sector issues.

Looking ahead, growth can be expected to rebound strongly after a relatively short, but sharp, weakening of economic activity, and a rapid narrowing of external deficits. In fact, we are already seeing improvements in exports, even though recent exchange rate changes have not had much opportunity yet to generate their effects. And as these adjustments take place, each of these countries will be embarking on a longer-term process of structural change that will strengthen their economies in fundamental ways—such as by restructuring their financial systems, increasing domestic competition, and otherwise improving the climate for productive investment and high, but sustainable, growth. That is why I believe that these economies will emerge from this period stronger and more dynamic than before.

What can you, as the business leaders of your countries, do to advance this process? The region has entered a period of slower growth, but with forceful action to tighten macroeconomic policies and forge ahead with financial sector restructuring and other structural measures, confidence can be restored sooner rather than later.

One important way in which you can help shorten the period until stronger growth resumes is by helping to improve transparency—for example, by complying with "best practices" in accounting standards in the corporate sector, and by avoiding "connected lending" and other practices that raise doubts about the strength of corporate governance and the links between government, banks, and industry. Such steps will help convince markets that your countries do indeed embrace reform and that they have the resolve to put current problems behind them.

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Africa: A Continent on the Move

Thank you for giving me the honor of speaking with you on the occasion of this Summit of the Organization of African Unity. I am all the more conscious of this honor because this meeting is taking place at this particular point in time. Despite all the tragedies besetting it, Africa is moving forward. Economic growth has resumed in most of the continent, and your countries are reaping the fruits of implementing sound economic policies.

With many of you, we have already started thinking about a new generation of reforms that will enable you to accelerate progress and growth, and more quickly win the war against poverty. But now the strength and magnitude of the Asian crisis seems to have called everything into question. The IMF is working to contain this fire and put it out, and to help the countries concerned to emerge stronger from the ordeal. I thus felt that the best I could do—in responding to the concerns that this crisis has raised in your minds—would be to share with you my thoughts, while they are still fresh. Once again, it is a question of globalization, of the opportunities and risks for the emerging countries and for your countries, as well. It is also a question of what actions will be required of Africa's development partners, bearing in mind the progress that has been achieved in recent years.

* * *

Africa's Recent Progress

After two decades of lost opportunities, Africa's economic performance has improved and the outlook has brightened. Together with President Mugabe we can speak of a "Renaissance of Africa." Real GDP for the region as a whole is growing at an annual rate of 4–5 percent, and per capita incomes are on the rise. African coun-

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Address at the Summit of Heads of State and Government of the Organization of African Unity, Ouagadougou, Burkina Faso, June 9, 1998.

tries—especially those pursuing programs supported by the IMF, the World Bank, and the African Development Bank—are increasingly partaking in the economic recovery. In the early 1990s, fewer than 20 enjoyed growth rates of 3 percent or more. But by 1997, the number of countries had doubled to about 40. Inflation has also come down sharply—with the average rate falling from a peak of close to 36 percent in 1994 to about 10 percent in 1997. Fiscal deficits have been cut by half in the past five years and external current account deficits, after widening slightly in the mid-1990s, were down to 2.5 percent of GDP in 1997. All this constitutes a remarkable reversal of the trend: from a constant drift toward poverty toward continuous positive per capita growth rates.

These improvements do not warrant euphoria, but they should encourage us to look to the future with optimism. We can be confident, because they are attributable not to luck but to better economic and financial policies in Africa—that is, to your own rigorous efforts and the many initiatives to promote good governance, develop human resources, ensure respect for human rights, and democratize political regimes.

The New Environment

Yet, despite this progress on so many fronts, Africa's growth performance still lags behind that of many developing countries. Thus, it is essential to build on these gains and to make endemic poverty retreat. How can we do this in such an unpredictable international context? It is here that we must interpret correctly the messages coming to us from Asia. We should read them not as a sign to reject globalization, but rather to reject the mistakes that were made.

Globalization offers access to a larger volume of financial savings, a wider range of goods and services at lower costs, new export markets, and new technologies. That is the positive side! Such opportunities can lead the way to higher productivity, faster growth and development, higher living standards, and lower poverty. And with market integration proceeding rapidly, Africa must open up and compete if it is to take advantage of the benefits of this process. But globalization also poses two important risks. First, for countries that are slow to integrate into the world marketplace, the risk of marginalization. Second, when investors—domestic or foreign—abruptly

lose confidence, the risk of capital flows drying up or reversing, thereby precipitating a crisis. That is the negative side!

So what exactly happened in Asia? Certainly, the "Asian miracle" underscores the fact that high savings, investing in human and physical capital, and liberalizing the economy pay off in terms of growth. But the key lesson of recent events is that pursuing these policies alone is not enough. Good economic governance must be maintained at all times. Yet in all of these countries, there were lapses. The soundness of the banking system in particular is something that must be monitored all the time. But in some countries, it only appeared to be happening. Finally, great care must be taken to ensure that the government conducts its affairs in an irreproachable and transparent manner and that all forms of corruption, favoritism, nepotism, and, if I may use the expression, "cronyism" are shunned. Yet over time, in Asia, these tainted practices overpowered systems that were otherwise remarkably successful.

But let us not blame the Asian countries. These blemishes exist everywhere, and these countries' problems would not have reached such proportions if the financial institutions of certain industrial countries had not been irresponsible as well. But the lesson remains: it is now clear that all reform programs should promote transparency and accountability in government and corporate affairs. Indeed, the golden rule for a globalized world, Mr. Chairman, is transparency. It is also to strengthen banking systems; to level the playing field for the public and private sectors; to liberalize capital flows in a prudent and properly sequenced way; to eliminate unproductive government spending; and to combat all forms of bad management and favoritism. These are the harsh lessons that the Asian experience suggests.

It is in this new world environment that Africa must now frame its economic policies and accelerate its growth. But it cannot do it alone. And it is against this backdrop that Africa, the industrial countries, and the multilateral institutions must join forces in a world partnership that, so far, is taking shape all too slowly. So what should our agenda be?

An Agenda for Africa

Let me begin with what you need to do. You need to prepare your own strategy. May I suggest to you some elements of that strat-

egy that would enable you to maximize the benefits of globalization while avoiding its perils. I am merely suggesting priorities that you have often discussed—and that are already reflected in the actions that many of you have taken.

- First, consolidating macroeconomic stability. Africa must now redouble efforts to reduce inflation to sustained low rates and ensure the viability of the external position. At the same time, fiscal efforts should focus increasingly on the quality and composition of public expenditures. In this way, saving will be promoted and high-quality growth encouraged. In your budgets, spending on health, education, agriculture, welfare, and basic infrastructure will override unproductive outlays, including military spending (in this area, I fully support the guidelines proposed in April 1998 by the Secretary-General of the United Nations).
- Second, ensuring economic security—removing the sense of uncertainty that still too often plagues investor decision making in Africa. The direction and implementation of economic policies must be beyond question, as must competence, integrity, and judicial independence. Moreover, the transparency, predictability, and impartiality of the regulatory and legal systems must be guaranteed. This goes well beyond the respect of private property rights and the enforcement of commercial contracts. It also involves the elimination of arbitrariness, special privileges, and ad hoc exemptions, even when these are intended, mistakenly or shortsightedly, to encourage investment.
- Third, strengthening the financial sector in order to better mobilize savings and deepen financial intermediation. Critical elements should include an independent central bank aiming at price stability, with autonomy and transparency in the conduct of monetary policy; sound banking practices; prudential supervision free of government intervention; and a well-functioning payments system.
- Fourth, speeding up trade liberalization to boost the efficiency and competitiveness of domestic producers. This should include the elimination of nontariff barriers and monopolies, and a major reduction in import and export duties, both of which raise the costs of doing business and hamper

Africa's integration into the international economy. Moreover, trade liberalization and a more transparent trade regime play an essential role in enhancing the investment climate.

- Fifth, at the regional level, fostering efficient forms of economic cooperation and integration. To be convinced of the usefulness of such multilateral liberalization, we need only remember that there are more than 20 countries in Africa with fewer than 10 million inhabitants, and 15 countries that are landlocked—yet a major share of Africa's foreign trade is with the rest of the world. In this connection, Mr. Chairman, what could I possibly add to what you stated so well yesterday?
- Sixth, ushering in an era of good governance. National authorities should spare no efforts to tackle corruption and inefficiency, and to enhance the accountability of all public administrators.
- Seventh, continuing the broad, frontal attack on structural problems, while keeping a central focus. Strengthen everything that might encourage private investment and the entrepreneurial spirit at all levels in order to create the closely knit network of small and medium-sized enterprises that will create tomorrow's jobs and opportunities.

Seven priorities for Africa's development—all of which you have been talking about for some time, and some of which are in place in some of your countries. But if the world and your countries could see you adopt all seven of them together, then this image of a lagging Africa, an Africa that is ambivalent about development, an Africa that is, in the words of President Compaoré, a "champion of the negative indicators"—this image will at last be replaced by the one you want to create: an Africa that is actively catching up, open, enterprising, at peace, and sure of its destiny.

An Agenda for the Industrial Countries

How about the more advanced economies? What can they do to help Africa?

- First, the largest industrial countries have a particular responsibility to *promote world economic growth and stability*

through the excellence of their own economic policies, and by cooperating to minimize potential sources of instability in the global economy.

- Second, industrial countries should do more to *open their markets* to products in which African countries have, or are likely to develop, a comparative advantage—including processed agricultural products, mineral products, and manufactures such as clothing and footwear. They also need to phase out subsidies on their agricultural exports more quickly than currently planned.
- Third, donor countries must *strengthen their bilateral assistance* to countries that have demonstrated a commitment to reform—particularly in areas where a bold approach to reform might involve important, albeit transitional, immediate costs but durable longer-term gains, such as comprehensive trade, civil service, and parastatal reform. A first, essential step would be reversing the declining trend in official development assistance; I deplore the profound and distressing silence that currently surrounds this issue. And here, this bears repeating: there are essential tasks for which the private capital inflows made possible by globalization will never be able to replace official development assistance, particularly in grant form. At a time when Africa's orderly integration into the global economy is such a high-stakes issue, not only for Africa but for the world, it would make precious little sense to refer to "donor fatigue."
- Fourth, industrial—and developing countries—need to *strengthen efforts on combating corruption*. A key step would be ratifying the OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions.
- Fifth, industrial and other economically more advanced countries must *ensure that the multilateral institutions have the necessary resources* to promote and support adjustment efforts and, in general, fulfill their increasingly complex tasks. Let us discuss these tasks for a moment, particularly the reforms that the IMF wishes to undertake to serve Africa better.

An Agenda for the Multilateral Institutions

Exactly how can the multilateral institutions help Africa? Here, I would like to discuss what the IMF plans to do. We are now focusing our efforts on five key initiatives.

- First, the IMF is taking steps to put the Enhanced Structural Adjustment Facility (ESAF)—its facility for loans at an interest rate of 0.5 percent—on a permanent footing so that we can continue to support your reform efforts over the long term. This involves securing the necessary resources to ensure that the ESAF, which was begun as a temporary facility some 10 years ago, will be self-sustaining by 2005, and thus remain available in perpetuity. In Africa today, 22 countries, out of a total of 40 ESAF-eligible ones, are pursuing ESAF-supported reform programs—with a total commitment of financial assistance of about $3.6 billion.

  Moreover, we want the ESAF to serve you better. We have reflected on our successes and failures. I, myself, consulted a number of you. Then we asked a group of experts headed by Dr. Botchwey, the former Finance Minister of Ghana, to assist us in identifying reforms that would ensure that each of our new programs can trigger more rapid and socially oriented growth that no longer stops at today's ceiling of 5–6 percent, which is far from negligible, but that can reach and surpass the 7 percent level. This will be achieved not with less reform and adjustment but with better reforms and more rigorous adjustment. Which is why we want to help governments take ownership of programs that they can truly call their own and firmly stay the course on reforms. For that reason, we wish to strengthen our collaboration with the World Bank to improve the quality of the assistance that our two institutions can provide. Together, we shall take a fresh look at ways to accelerate public enterprise and financial sector reforms; improve the assessment of medium-term investment needs and capacity to absorb external financing within your countries; and identify potential adverse social consequences of reforms, to be in a position to coordinate with you appropriate, rapid, and effective responses to the problems involved.

Finally, we must assist those countries that are furthest along in the reform process to succeed to the fullest, eventually to be able to forgo our financing as they will have gained access to international markets on favorable terms. We are looking into precautionary arrangements that would clearly indicate to financial markets that the Fund endorses and closely monitors their economic policy. This should be of considerable help to private investors in proceeding with favorable investment decisions.

- Second, together with the World Bank, we have been moving swiftly to implement the debt initiative for the heavily indebted poor countries (HIPCs). Just in the 18 months since the launching of the HIPC Initiative, commitments to provide assistance under the Initiative of about $6 billion have been made to six countries: Bolivia, Burkina Faso, Côte d'Ivoire, Guyana, Mozambique, and Uganda. Also, preliminary discussions are under way for Mali and Guinea-Bissau, and over the coming year, we hope to consider a number of others, including Mauritania and Ethiopia—assuming that these countries persevere in their adjustment and reform efforts.

The HIPC Initiative may strike many as timid. It does have its limitations, for it calls for a very broad consensus on the part of creditor countries, which may not in fact share the same assessments of the situation or the same priorities. The HIPC is, nonetheless, an opportunity for Africa, and Africa must seize this opportunity to expeditiously reach a sustainable external debt position. So I call on all eligible countries to take the needed policy measures with all possible speed so that they can take advantage of the debt initiative. The list of beneficiaries could be much longer, as we all hope it will be by 2000.

We are also weighing changes that would allow for a more flexible response to the exceptional needs of the postconflict countries. And we welcome calls issued in many recent forums, such as the Group of Eight Birmingham Summit, that the creditor countries—the ones that may not already have done so—forgive aid-related bilateral debt or take comparable action. We also welcome calls that new bilateral assistance be provided in the form of grants to these countries, and

that export credit agencies lend only to finance expenditures that are productive.

But, as you well know, debt is only one of the impediments to sustainable development. The countries that wish to solve this problem in the absence of an appropriate policy framework cannot hope to achieve much. That is precisely why we have stressed all along that debt relief under the HIPC Initiative be linked to programs that can act as a catalyst for high-quality growth and help position countries to tap international capital markets in due course.

- Third, over the years, the IMF has provided assistance to countries that have experienced political turmoil, civil unrest, or international armed conflict—and since 1995, we have had a special policy to provide emergency postconflict assistance. Rwanda is the first African country to benefit from this new policy, with two loans of about $20 million approved in 1997 in support of the government's economic program. The Republic of Congo may be next in line, and we are also having discussions with Angola.
- Fourth, the IMF stands ready to continue to provide—and intensify—our training and technical assistance for capacity building and institutional reform in Africa. Perhaps one of the most encouraging signs is the recent Initiative of the African Governors of the Bank and the Fund to ensure that capacity building is henceforth an integral part of Africa's development agenda. In this context, the IMF Institute has been expanding its training activities for African officials and supporting regional training and research institutions. It is our intention to extend the reach of our training by the establishment of an IMF regional institute in Africa, jointly with training partners in the region.
- Fifth, we are particularly mindful of Africa's situation as we consider how best to help shape a new financial architecture so that the global economy will be less prone to financial crises. As more and more countries in Africa tap the international capital markets, as I trust they will, we would like them to face as favorable and secure an environment as possible. To this end, we will be pursuing approaches that include improving the availability and transparency of information, and

developing and disseminating new standards and best practices, which should help to promote greater overall stability. Africa, its Executive Directors, Governors, and Ministers must play an active part in these efforts. It is essential that Africa's voice be heard as these efforts unfold.

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Well, as you can see, this is an ambitious agenda for all of us. I could propose no less, Mr. Chairman, in response to your desire for this summit to help Africa face the challenges of the twenty-first century. Indeed, it is an agenda well worth pursuing as the spirit of hope and progress sweeps across Africa. Moreover, I am confident that as broader-based progress gathers momentum, the image of the new, emerging Africa will soon take hold. And we, at the IMF, will do our part to help make that a reality.