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In this issue

The next issue of the *IMF Survey* will be published on September 2.

NBER speech

Krueger says Argentina needs sustainable monetary anchor, stronger banking system

On July 17, IMF First Deputy Managing Director Anne Krueger addressed a National Bureau for Economic Research (NBER) conference on the lessons to be learned from the Argentina crisis and how these can be used to raise the effectiveness of IMF efforts to prevent and resolve financial crises. Following are edited excerpts from her remarks; the full text is available on the IMF's website (www.imf.org).

Ordinary people in Argentina are paying an enormous price for the current crisis, and it is incumbent upon us in the international community to do all we can to help the country recover as quickly as possible and to help prevent other countries from suffering a similar fate.

What went wrong in Argentina? In hindsight, it is clear that fiscal policy was too weak during the upswing; the external environment and shocks were unfavorable; the convertibility plan locked in overvaluation, given the lack of flexibility in the domestic economy; and unsustainable debt dynamics were left unaddressed. In other words, Argentina became caught in a vicious cycle of weak activity, overvaluation, and mounting debt.

Lessons for crisis prevention, resolution

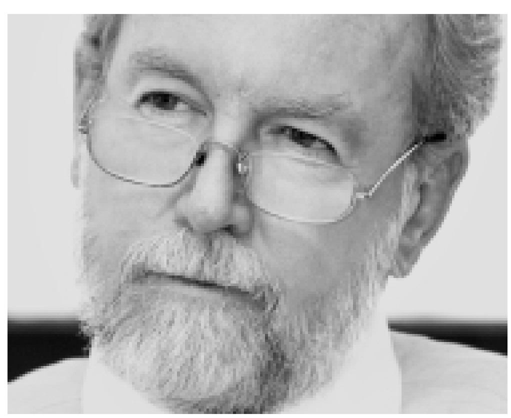
Bearing in mind that Argentina *did* apply many of the lessons that the international community thought it learned from the Mexican and Asian crises, what more have we at the *(Please turn to following page)*

Interview with Jack Boorman

Better institutions and good policies hold keys to avoiding financial crises

In December 2001, Jack Boorman stepped down as IMF Counsellor and Director of the IMF's Policy Development and Review Department, capping a 27-year career at the IMF. He spent much of the 1990s on the front lines of financial crises in Asia, Russia, and Latin America and, in the wake of those crises, helped develop many of the initiatives aimed at strengthening the global financial system. He was also a major force in shaping the IMF's various loan facilities, including those developed to help the poorest countries. Laura Wallace speaks with Boorman, now a part-time Advisor to the Managing Director, about his reflections on a distinguished career.

IMF Survey: In recent years, the IMF has come under unprecedented criticism. What's your reaction, including to the latest criticisms by Professor Stiglitz? *(Please turn to page 245)*



Boorman: "How globalization proceeds is by no means foreordained. It depends on how it's managed."

What probability of success should we look for before we lend: 40, 60, or 80 percent?
—Anne Krueger

Krueger on lessons from Argentina

(Continued from front page) IMF learned—or relearned—from Argentina's own experience?

First, we should have focused more closely on the debt dynamics. Indeed, we are now stepping up our work on the analysis and assessment of debt sustainability (bearing in mind, however, that this will always remain fundamentally a matter of judgment). In Argentina, assessing the implications of the debt position was complicated by the fact that confidence in debt sustainability and the maintenance of the currency board were intertwined. Doubts about one threatened potentially self-fulfilling concerns about both.

Second, currency boards are not necessarily as durable as some people liked to imagine in the wake of the Asian crisis, especially if they lack support from accompanying fiscal and structural policies. One of our priorities in strengthening surveillance is to be more candid and comprehensive in our analysis of exchange rates and exchange rate regimes.

Third, emerging market countries may need to be even more conservative with public external debt than we had thought. If a country's private sector is benefiting from access to international capital markets—which is all to the good—then it is dangerous for the public sector to rely on it too much for cheap finance as well. Changes in international capital markets have already forced us to change our rules of thumb for the adequacy of official reserves. A similar rethink may be required here.

Fourth, we need to make it easier for countries to exit in a timely fashion from unsustainable debt dynamics. Restructuring unsustainable sovereign debts has become more difficult since the 1980s, with the shift from syndicated bank loans to bond issues. Creditors have become more numerous and diverse, creating problems of coordination, collective action, and intercreditor equity when restructuring becomes necessary. With 88 bond issues outstanding, Argentina is a good example. Hence our proposal for a sovereign debt restructuring mechanism that would empower the debtor and a supermajority of creditors to make the key decisions in a restructuring in a timely and efficient way. Perhaps if such a mechanism had been in place, Argentina's debt time bomb could have been defused a few months before it finally blew up.

Fifth, we need to make our policy advice more persuasive when times are good and members do not require our financial help. This means closer dialogue with policymakers and more outreach to the wider community. But, as I noted earlier, there is a limit to how persuasive one can be when private money is pouring in.

Overarching these lessons is a bigger and even more difficult one. In a way, it is the IMF's eternal dilemma: how far should we go in supporting a policy strategy to which the authorities are deeply committed, but that we and investors doubt may succeed? What probability of success should we look for before we lend: 40, 60, or 80 percent? And how should one trade off the strength of a potential program against the chances of successful implementation? These judgments all have to be made in conditions of great volatility and uncertainty, both economic and political.

Ownership by the authorities—and ideally by society more broadly—is very important if a program is to be implemented effectively. If we had forced the authorities in Argentina to abandon the convertibility plan and/or default on their debt, then we would have been blamed for the economic consequences. More important, the resulting lack of ownership and commitment by the authorities would likely have made those consequences more severe in their impact on the Argentine people. (National policymakers are just as aware of this dilemma as we are, of course, which can encourage a measure of gamesmanship in the negotiation process.)

We must remember that while ownership is necessary for the success of a program, it is not sufficient. It has to make sense economically. At the end of the day, a country is responsible for the policies it chooses—and we are responsible for deciding whether to lend in support of them.

The whole point of IMF lending in financial crises is to take risks and provide finance where the private sector will not, but at the same time we are responsible to our members for ensuring that their money restores growth and viability, thereby allowing repayment. Some people will always—and do always—complain that we err too much on one side or the

Selected IMF rates

Week beginning	SDR interest rate	Rate of remuneration	Rate of charge
July 22	2.29	2.29	2.93
July 29	2.25	2.25	2.88

The SDR interest rate and the rate of remuneration are equal to a weighted average of interest rates on specified short-term domestic obligations in the money markets of the five countries whose currencies constitute the SDR valuation basket. The rate of remuneration is the rate of return on members' remunerated reserve tranche positions. The rate of charge, a proportion of the SDR interest rate, is the cost of using the IMF's financial resources. All three rates are computed each Friday for the following week. The basic rates of remuneration and charge are further adjusted to reflect burden-sharing arrangements. For the latest rates, call (202) 623-7171 or check the IMF website (www.imf.org/cgi-shl/bur.pl?2001).

General information on IMF finances, including rates, may be accessed at www.imf.org/external/fin.htm.

Data: IMF Treasurer's Department

other. That is inevitable, but we need to be as clear and open-minded as we can be in explaining and justifying the decisions we make.

Immediate challenges

Let me conclude by talking a little about the immediate challenges Argentina faces now. You will appreciate that I am somewhat constrained in what I can say here. The economic situation remains very difficult.

- Real GDP was down more than 15 percent in the first quarter compared to a year earlier, although recent data show industrial production possibly bottoming out.
- Inflation continues to rise, with consumer prices increasing by 30 percent and wholesale prices by almost 100 percent in the first six months of the year.
- Liquidity assistance to banks has dramatically expanded the monetary base, with the year-on-year change in currency issue moving from minus 27 percent in December to plus 26 percent by the end of June.
- The fiscal position remains weak, although improving, with the consolidated primary budget deficit standing at around 1 percent of GDP in the first half.
- Despite a current account surplus, intervention to reduce pressure on the peso and inflation is depleting official reserves.

We have seen some welcome progress in key policy areas, including satisfactory amendments to the insolvency law and the repeal of the economic subversion law. The authorities are also making progress in putting in place bilateral agreements with the provinces to ensure an orderly adjustment of their finances. This is an essential component of a coherent fiscal framework.

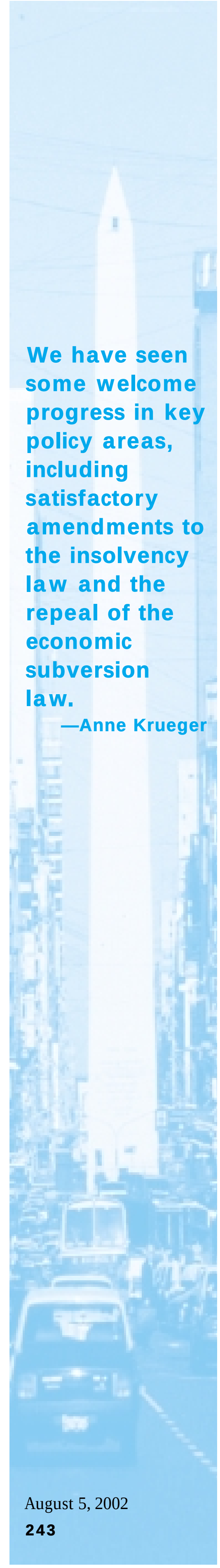
Reflecting this progress, the IMF's Executive Board agreed on July 15 to extend by one year the expected repayment of $985 million due from Argentina under the Supplemental Reserve Facility.

Our discussions with the authorities will now focus on two key areas.

First, developing a sustainable monetary anchor, which has been lacking since the abandonment of the currency board. This is essential to halt rising inflation. The recently appointed independent advisory group [see box below] will provide valuable assistance here. One issue they and we will have to address is the outcome of the voluntary securitization of bank deposits that was initiated with the lifting of the *corralito*. Another important question is how best to restore the independence of the central bank, which is essential to long-term confidence.

Second, strengthening the banking sector. The key elements here are a framework for bank intervention and resolution; a consistent and sustainable liquidity support policy; and proposals to reform, restructure, and downsize public banks. The authorities expect to detail their plans here shortly.

Rapid progress in these and other areas is essential to create a strong and comprehensive program with the capacity to restore confidence, underpin a sustained economic recovery, and win international support. We will remain fully engaged with the authorities in working toward that goal. ■



We have seen some welcome progress in key policy areas, including satisfactory amendments to the insolvency law and the repeal of the economic subversion law.
—Anne Krueger

Independent advisors suggest broad principles for handling issues facing Argentina

IMF Managing Director Horst Köhler on July 29 welcomed the report "Economic and Financial Issues Facing Argentina," presented by the Panel of Independent Advisors (see *IMF Survey*, July 22, page 225). The panel was established to assist Argentina in addressing the complex challenges it faces on the economic and financial fronts: output and employment are depressed, the normal functioning of the banking system has been disrupted, the government is unable to service its debts, and substitute quasi currencies are circulating throughout the economy. "The views and conclusions of the panel," Köhler said, "will be very helpful to the Argentine authorities and to the IMF as we continue our discussions toward an economic program for Argentina that will restrain inflation, restore macroeconomic stability, and put the economy on a path of recovery."

Köhler noted that the report "underlines the need for a credible monetary anchor that gives the authorities the clear capacity to limit the creation of peso liquidity to the demand to hold pesos." It also emphasizes that adequate monetary control cannot be exercised without an early and permanent solution to the problem of the court-ordered releases of deposits (the *amparos*).

The report cautions that restoring macroeconomic stability will also depend on ensuring central bank autonomy, implementing a strong fiscal program, ending the issuance of provincial quasi currencies, and working with the banking system as a full partner in Argentina's recovery.

Köhler concluded that the IMF had "already planned to continue its dialogue with the authorities in all these areas in the period ahead, with a view to putting these policies in place and moving toward an IMF-supported program, as soon as the authorities are in a position to ensure their implementation."

For the full text of the report by the advisory panel, see News Brief 02/80 on the IMF's website (www.imf.org).

Central American conference

Regional IMF surveillance, policy priorities topped agenda for high-level financial meeting

In recognition of the region's growing economic interdependence, the Central American Monetary Council and the IMF on July 25–26 convened a conference in La Antigua, Guatemala, to discuss regional surveillance of the area's economies and the policies needed to ensure macroeconomic stability and higher growth. The high-level meeting drew presidents of central banks, ministers of finance, and bank supervisors from Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and Panama. Also attending were representatives from the World Bank and the Inter-American Development Bank.

IMF Executive Director Hernán Oyarzábal (left) addresses the conference. On the right is Guatemala Finance Minister Eduardo Weyman.

Over the past decade, increasing trade links within the region and growing globalization of financial markets have made it clear that Central American countries could benefit from the IMF's annual evaluation (surveillance) of its economic policies on a regional as well as a national basis. Regional surveillance offers an opportunity for expanded dialogue with the IMF on domestic policies and international developments within a regional context. Such discussions would address macroeconomic risks and propose the appropriate design and coordination of policy responses.

Participants focused on six topics of major concern to the region: the sustainability of public debt; the design of efficient and equitable tax and expenditure policies; the choice of exchange rate regime; the supervision of the financial sector; the outlook for external trade; and the impact of the decline in international coffee prices.

A theme running through the discussions was the need to lay the basis for continued growth and stability in a region traditionally vulnerable to external shocks and likely to see significant changes in its production and employment patterns if a trade agreement is reached with the United States. There continues to be a pressing need, too, for reduced poverty and economic inequalities.

Participants pointed to specific steps that could be taken to reduce economic vulnerabilities—chiefly lowering fiscal deficits, limiting the growth of public debt, and significantly strengthening the supervision of the financial sectors. In the short term, however, they emphasized how important it would be to gear both fiscal and monetary policies to support current exchange rate regimes.

There was also broad agreement that public spending on basic health care and primary education represented a critical element in combating poverty and that further investment in infrastructure would be needed to strengthen growth prospects. To provide resources for such public spending, participants agreed that the countries of Central America would need to increase tax revenues, in part by simplifying tax systems and improving tax administration and enforcement. ■

Francisco Baker
IMF External Relations Department

Köhler and Wolfensohn call for aid for southern Africa

Responding to a deepening food crisis in southern Africa, IMF Managing Director Horst Köhler and World Bank President James Wolfensohn called on donor nations to provide critically needed food aid and financial support to the region. In a joint letter on August 1 to their Executive Boards, they underscored the urgency of the situation, noting that conditions were expected to deteriorate rapidly over the coming months and that up to 13 million people would likely require sustained food assistance.

The letter was issued in support of the United Nations' appeal, launched on July 18, to provide $611 million in humanitarian relief for the 14 member countries of the Southern African Development Community. "We stand ready to support emergency financial assistance to the region," Köhler said, adding that in countries that have IMF-supported programs, "we have been discussing possible augmentation of existing loan arrangements to help fill gaps between donor assistance and actual financing needs. We also have resources available that can be put to use under the IMF's Compensatory Financing Facility and Emergency Assistance Facility."

Köhler and Wolfensohn acknowledged that initial pledges to the UN appeal did not yet cover a significant proportion of the funds required and called upon their Executive Board Directors to "make a specific and urgent request to aid agencies and development partners of the members of your constituency to deliver additional support through the international appeals. We pledge ourselves to ensure that the IMF and the World Bank, through technical and financial assistance, also continue to play their part in mitigating this humanitarian crisis."

For the full text of News Brief 02/81 and the letter to the Executive Directors, please see the IMF website.

Boorman responds to the IMF's critics

(Continued from front page)

BOORMAN: This wave of criticism has been one of the great disappointments of my time at the IMF. It was particularly difficult to live with in the midst of the Asian crisis—partly because I felt that the extent and intensity of the criticism affected some countries' steadfastness and willingness to go ahead with some of the needed reforms. Perhaps if there had been less challenge to some of the IMF's basic advice—such as tightening monetary policy and using interest rates to defend the exchange rate—the authorities would have been more aggressive in the initial stages. I believe that if they had been, stabilization might have occurred earlier, and, perhaps, growth would have rebounded even more quickly. That said, most commentators, and indeed even some critics, are now seeing, with the rather rapid and impressive recovery of Korea and most of the other crisis countries, the necessity, and even the wisdom, of some of the reforms the IMF had pushed. On this subject of monetary policy and interest rate management in crises, I think Stiglitz's commentary in his book is simply wrong. Little empirical evidence has been found to support his views.

IMF SURVEY: Should the IMF have given Stiglitz more of a hearing?

BOORMAN: If you mean with regard to his recent book, I endorse the thrust of the remarks made by [IMF Economic Counsellor] Ken Rogoff [see "Rogoff's discontent with Stiglitz" in the July 8 issue of the *IMF Survey*]. I was a bit surprised that Stiglitz thought those remarks an unfair personal attack. His book itself represents a personal attack on many people, including much of the IMF staff.

As to whether he was given a fair hearing during the Asian crisis, he was, after all, the World Bank's Chief Economist at the time. That is a very visible position. He had many forums, both inside and outside the Bank, to give his views. And he did. And we heard him. But we disagreed. Interestingly, he complains that the U.S. Treasury didn't listen to him properly when he was head of the Council of Economic Advisers and that the U.S. Treasury and the IMF didn't listen when he was Chief Economist at the Bank.

IMF SURVEY: Should the IMF have handled the Asian crisis differently?

BOORMAN: I believe the general thrust of our advice was correct. Could some things have been done differently? There's no question. We've learned a lot and, of course, hindsight helps both us and the critics. Besides more aggressiveness and consistency on monetary policy in all of the Asian crisis countries, an early move to a blanket deposit guarantee in Indonesia—rather than the partial one put in place when the initial 16 banks were closed—might have avoided a deposit run. A blanket guarantee could have allowed even more banks to be closed—something that was called for—without creating a major loss of confidence in the banking system. That, in turn, might have facilitated a quicker reform of the banking system. We also could have done better at dealing with the systematic collapse of the corporate sector.

IMF SURVEY: Some critics charge that we're making the same mistakes in Argentina.

BOORMAN: Argentina is very different. Its problem stems much less from difficulties in the private sector and much more from a classic fiscal problem in the public sector—not just at the central government level but also at the provincial government level, something that is extremely difficult to deal with. When a country adopts a currency peg or a currency board–like regime, such as the one Argentina adopted, the constraints on other macroeconomic policies—monetary and fiscal—are extremely demanding. In Argentina's case, the fiscal demands simply weren't met.

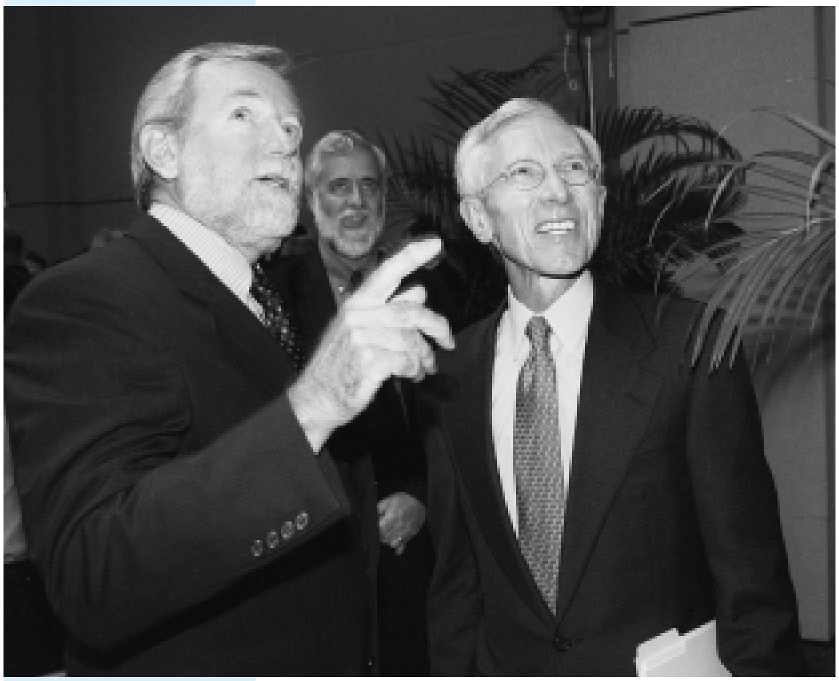
Jack Boorman with former IMF Managing Director Michel Camdessus.

Michael Mussa [former IMF Economic Counsellor] has just put out a well-done piece on Argentina for the Institute of International Economics. His profile of fiscal policy, especially when the country was doing rather well between 1996 and 1998, shows that policymakers did not use that period of rapid growth to improve the fiscal situation—and probably the IMF did not press them hard enough to do that! Fiscal deficits persisted, increasing the outstanding stock of debt and sowing the seeds for later problems. These problems were aggravated when Argentina was hit by some adverse external factors—the strengthening of the dollar, the devaluation of the Brazilian *real*, and the slowdown in the global economy.

IMF Survey: Mussa says the IMF blundered by continuing to lend to Argentina in September 2001.

Boorman: That's where I part company with him. I believe that his analysis omits a number of elements that influenced the IMF's decision to provide one more opportunity for Argentina to correct its problems.

First, over the course of the past decade, Argentina had made enormous progress in restoring the rule of law and the sanctity of contracts. That was a major achievement after decades of abuse, and it was worth protecting. Unfortunately, recent actions, including the deposit freeze, have reversed that progress at great cost to Argentine society.



Jack Boorman (left) with IMF Deputy Managing Director Eduardo Aninat (center) and former First Deputy Managing Director Stanley Fischer.

Second, the official community needs to be very careful when it decides to withdraw support from a crisis country. Clearly, Argentina needed debt relief. But there are, at present, no systems or mechanisms to provide confidence that the country and its creditors can agree, in a reasonably orderly way, on the debt relief the country needs. Fortunately, a substantive discussion has now begun to find a means—through either collective action clauses or a sovereign debt restructuring mechanism—to deal with such situations.

Third, fiscal decentralization creates novel problems for the central government and political leaders, and decisions had to be made about what those leaders could deliver. In the end, we decided to support their commitments, but they quickly fell short of what was needed.

Finally, Argentina was the largest emerging market borrower. One could not be unconcerned about the impact of a default by Argentina on that market.

IMF Survey: Would a sovereign debt restructuring mechanism really make a difference? And will it ever be politically accepted?

Boorman: I'm sure that whatever specific proposal is ultimately put forward, it will be a difficult sell in a number of countries because it will involve some ceding of judicial authority from national courts to an international forum. But it's important that discussion not be closed off just because, at the outset, the proposal may appear politically infeasible. We need to see the discussion through to the end, determine the best approach, and then try to sell it politically if we believe it will deliver. To the great credit of the First Deputy Managing Director [Anne Krueger], she has managed to catalyze the most substantive discussion on private sector involvement that has taken place in many years.

IMF Survey: You were the IMF's resident representative in Indonesia from 1976 through 1978. It must have been extremely difficult to watch it go through the wrenching experience of 1997–98.

Boorman: Most people who know me know that I left some part of my soul in Indonesia. So, obviously, I was pained by what I saw. Indonesia is perhaps the most evident case of a country's economy growing so rapidly and increasing in sophistication so fast that it simply outgrew its institutions. The tragedy is that President Suharto—who had overseen a dramatic economic transformation—could not see the ramifications of the apparently free rein he was giving to his family and some of his friends to exploit their connections to the palace.

By this, I don't mean just the monopolies, which obviously exploited opportunities for rent seeking in the country, but also the creation of an atmosphere where the rule of law became subverted. For example, how are regulators in the banking sector supposed to do their job when, at every turn, they fear stepping on the wrong toes? When this thinking becomes pervasive, it is inimical to the kind of supervision and regulation that's required in an increasingly complex economy.

The failure—and I think this is the lesson we have learned from the crises of the past six or seven years—is not seeing clearly enough the demanding institutional requirements of a modern market economy. More effective institutions are what many of the initiatives on the architecture of the international financial system are all about!

IMF Survey: Do people need to take a stand for or against globalization? Do they have any power over whether it turns out to be a force for good?

BOORMAN: I believe that globalization is inevitable; the converse—a breakdown of the move toward greater integration—is too horrible to contemplate. But how globalization proceeds is by no means foreordained. It depends on how it's managed. We've learned a lot. We increasingly recognize, as I mentioned, the importance of institutional prerequisites for a modern market economy. I'm not talking about a laissez-faire economy, but one in which the government plays a key role in establishing the rule of law, the judiciary, the regulatory bodies, the supervisory agencies, the social safety nets, and the many other elements that make up the institutional infrastructure of a market economy. Indeed, the turmoil going on in the United States right now, and the argument over something as seemingly mundane as accounting standards, is a dramatic example of how important these systems are to the proper functioning of the economy.

There's also a greater recognition that if globalization is to work, you need robust international institutions with the power to set rules and arbitrate disputes. The World Trade Organization, the International Labor Organization, and other bodies have key roles to play. Of course, all countries in these organizations need to adhere to the rules, including—or perhaps most especially—the largest!

IMF SURVEY: As the world becomes more complicated, is the IMF changing the way it works?

BOORMAN: Much of what I spoke about regarding the critical importance of institutions and of systems in market economies has influenced the evolution of the IMF's responsibilities. In recent years, the IMF has moved heavily into new areas, including international standards and codes, assessments of financial systems, governance, and the like. We're putting out new products—such as Reports on the Observance of Standards and Codes (ROSCs) and Financial Sector Assessment Programs (FSAPs)—that are helping countries improve their systems and, increasingly, are being used by the private sector to assess credit risk. Recent surveys show that those countries that best adhere to these standards and best practices are beginning to see some rewards in terms of the spreads that they're paying on their international borrowing. These rewards are critical because, in my view, they are the major incentive for the adoption of best practices. However, it's disappointing that while many of these transparency initiatives were stimulated by the Asian crisis, some of the Asian countries themselves are lagging behind in signing on to them.

IMF SURVEY: You played a critical part in the mid-1980s in taking the IMF into structural and social issues. What made you feel the IMF needed to delve into this area?

BOORMAN: In recent years, we've been criticized for getting involved in structural adjustment, while in the early 1980s we were criticized for single-mindedly focusing on a country's macroeconomic profile and advising the compression of domestic demand as a means of adjustment without paying sufficient attention to growth.

The decision to pay more attention to the structural side of the equation was part of an effort to pay more attention to elements of the economy that would produce sustainable growth. That meant, among other things, developing institutions and removing distortions. Hence, we became more involved in building institutions in the areas of our expertise, like treasuries and finance ministries, or helping countries reform or create effective central banks. But we also became more involved in trying to correct some of the underlying problems, beyond the more narrowly defined macroeconomic ones.

The bottom line is that reform and adjustment are feasible and can be sustained with popular support only if the result is growth and an increase in living standards. Without bringing efficiency to the economy, without removing some of the distortions imposed by monopolistic practices or loss-making state enterprises, without improving governance, growth will eventually falter. As the economy changes, however, individuals may be hurt, and they will need help adapting to a dynamic market economy. This adaptation requires education, social safety nets, and other instruments to protect the vulnerable. Hence our concern with the development of such mechanisms. But this is not a job for the IMF alone. We can be effective only if all agencies with the requisite expertise work in concert to assist the developing countries.

IMF SURVEY: The structural adjustment facilities of the 1980s have evolved into the Poverty Reduction and Growth Facility [PRGF]. Two years after its launch, how's it doing?

BOORMAN: The PRGF emphasizes involving all segments of society—and not just the country's leaders—in formulating a poverty reduction strategy and the macroeconomic and structural policies that need to go with it. It also lays out the way in which the IMF, the World Bank, and others will work together to help the country. I've been pleasantly surprised by the level of commitment that this new approach has won in just two years, including from bilateral donors. My sense is that it will help ensure that all parties are pulling in the same direction and perhaps reduce the inefficiencies that can arise with a multitude of aid providers working in a country.

Recent surveys show that those countries that best adhere to these standards and best practices are beginning to see some rewards in terms of the spreads that they're paying on their international borrowing.

—Jack Boorman

The greatest contribution the IMF can make is to ensure that policymakers have access to the experience and lessons from other countries that have faced similar problems.
—Jack Boorman

IMF SURVEY: You seem to have been a firm believer in the expansion of IMF conditionality into a wide range of structural policies in the 1990s. Yet in recent years, you had to preside over the IMF's effort to pull back from much of that type of activity. How did you feel about the turnaround?

BOORMAN: The effort to streamline and focus conditionality originated in the criticism that the IMF went overboard in some of the Asian crisis countries. One question that, I believe, had an important influence on the debate was the extent to which countries have the capacity to deal with reforms on many policy fronts at the same time. Or, put differently, within the limited time frame of an IMF loan facility, how many major areas of reform can a country take on and hope to see effectively to conclusion, particularly when those countries increasingly have democratic systems in which decisions have to be debated and approved by parliament? I think that point alone convinced many people that—even if there is a desire to grapple with more issues and even if they're seen as desirable to the ultimate reform—there is a limit to what countries can tackle in one go.

Acceptance of that proposition has effectively changed the rules of the game and put the burden of proof on those who want to include more, rather than less, conditionality. And that is fine! At the same time, in my view, crises often present opportunities for reforms that would not be possible at other times. Failure to take advantage of those opportunities can mean significant loss to the economy—or additional crises. The trick is to find the proper balance. Over the past year, I think the IMF has succeeded in better concentrating conditions in areas that are clearly under its purview and in making sure the overall package is consistent with both the administrative and political capacity of the country. We're on the right track, but we need to be careful not to pass up the chance to help a government reform when that chance presents itself.

IMF SURVEY: What was your most satisfying experience during your years at the IMF?

BOORMAN: On a personal level, it was the opportunity to work with the people here, especially Michel Camdessus, Stan Fischer, Tom Leddy, and so many others, and the friends I've made both among the staff and with so many who have served on the Board. I can't imagine a more intellectually challenging atmosphere and one filled with better people. Frankly, I should be smarter than I am, because I can't remember a day that I didn't come to work and learn something from one of my colleagues.

In terms of the substance of the work, one small event that was enormously satisfying dates back to my days in Jakarta with Hubert Neiss: helping the Indonesians secure a better deal from the foreign oil companies after the major oil price increases of the mid-1970s. Not surprisingly, that deal greatly displeased the oil companies and the American ambassador in Jakarta at the time!

Over time, I suppose, the greatest satisfaction has come from helping to develop the various loan facilities of the IMF, especially those directed at the poorest countries. I believe these facilities have transformed the role and operations of the IMF—not necessarily with the support of, or to the liking of, all. But I believe it was right, and it has helped the IMF make a real contribution to the developing world.

IMF SURVEY: Going forward, what do you think the IMF's main priorities should be?

BOORMAN: First, we need to deal with the crises that a number of our countries face; obviously, Argentina tops the list.

Second, the IMF needs to be the center of expertise on macroeconomic policy and on those institutional and structural policies that fall within its purview. I'm not sure that we've developed the most effective systems to distill and disseminate the lessons of the vast experience the IMF sees in its member countries. I believe that policymakers seldom face problems that have not been seen, perhaps in a different guise, someplace else in the world. The greatest contribution the IMF can make is to ensure that policymakers have access to the experience and lessons from other countries that have faced similar problems. A top priority for IMF staff and the Board should be to serve as conduits for that experience.

Third, the governance of the IMF needs to be updated. The relative economic importance of countries has changed enormously over the past 25–30 years, and quotas have not evolved sufficiently. Countries like Korea and other Asian and developing countries should have a bigger voice. Europe's representation remains very large but no longer reflects the reality of Europe or of the European Union. Africa needs a bigger voice. But influencing the IMF is not solely a matter of quotas; it's also a matter of presence at the Executive Board, and that requires the best representation that countries can send.

Finally, the IMF's Board should be at the center of the discussion on all international financial issues. Too often, we see issues debated in outside forums and conclusions brought to the Board before it has had a full opportunity to put its own imprint on those conclusions. This is often neither efficient nor fair. That needs to change. ■

Per Jacobsson lecture

Ortiz: can the new financial architecture prevent emerging market crises?

On July 7 in Basel, Guillermo Ortiz, Governor of the Bank of Mexico, delivered a lecture cosponsored by the Per Jacobsson Foundation and the Bank for International Settlements entitled "Emerging Market Crises—What Have We Learned?" His remarks are summarized here; the full text is available at www.perjacobsson.org.

Since the devaluation of the Mexican peso in December 1994 and the ensuing financial crisis, emerging market economies have been subject to frequent crises. These crises share many features that distinguish them from those that struck emerging markets in the 1980s and early 1990s. What factors were behind these recent crises? What policies should emerging market crisis countries have pursued? Was the size of IMF packages adequate? Did these packages lead to moral hazard?

The recognition that countries with sound policies can be subject to speculative attacks has generated a wide discussion on the need to reform the international financial architecture. Ortiz discussed the reforms that have been proposed to reduce the frequency and negative effects of future crises and suggested additional improvements.

Liquidity or solvency crisis?

According to Ortiz, three issues have dominated the debate surrounding recent emerging market crises. First, did important fundamental imbalances trigger these crises, or were they the result of pure creditor panics? Most observers agree that the majority of these economies were subject to a dual crisis: a balance of payments crisis compounded by financial panic.

The policy response addressed the dual nature of the crises by implementing tight monetary policies and making available large international support packages to stop the run on the countries' assets. But, and this is the second issue, did these support packages create moral hazard? Although the theoretical evidence is thin, the IMF in particular was judged to have created moral hazard by setting an incentive structure in which investors did not pay due attention to default risk.

Third, did some of these episodes represent true solvency crises? If so, two elements are needed to combat this type of dual crisis: financing and adjustment.

Lessons from recent crises

The two most common features of the major emerging market crises of the 1990s were the enormous reversal in the capital account and the presence of some sort of fixed exchange rate arrangement. In the "classic example," continuing fiscal deficits financed with money issuance weaken a central bank's balance sheet, gradually depleting net international reserves until the monetary authority is no longer in a position to defend the domestic currency peg, which will then be successfully attacked by speculators. Private sector deficits, Ortiz emphasized, can also lead to persistent external imbalances and to eventual crises (as occurred in the Mexican (1994) and Asian (1997–98) crises). In the absence of prudential regulation and supervision coupled with a more open capital account, domestic banks provided credit to risky projects. The banks' unhedged positions suggested that several of these capital account crises were associated with important banking crises or had even been caused by them.

Ortiz: "The banks' unhedged positions suggested that several of these capital account crises were associated with important banking crises, or had even been caused by them."

Other elements that were present in recent balance of payments crises were contagion, institutional investment practices, and panic, or herd, behavior, Ortiz observed. The clearest case of financial contagion occurred as a result of the Russian crisis in 1998. This led to a substantial increase in sovereign bond spreads for a large number of emerging market countries, including, surprisingly, Latin America. Two years after the crises, the governments of these countries had returned to voluntary debt markets and faced terms not too different from those they had enjoyed prior to their crises. Therefore, the assumption that these crises were mainly liquidity ones was essentially correct.

Country policy dilemmas. Considering the need for a strong policy response, countries were confronted with some dilemmas, Ortiz said. The first one concerned basic decisions regarding monetary policy. After the fixed parities were abandoned, exchange rates plummeted in most cases. Central banks pursued a policy of high interest rates in the hopes of containing the extent of the depreciation and its inflationary effects. But high interest rates would hurt investment and cause further deterioration in economic activity. Moreover, a rising debt-service burden might also drive into delinquency those borrowers with local-currency-denominated debt linked to the floating exchange rate. Monetary tightening should therefore have been accompanied by additional fiscal tightening, and the tight policy response should not have been abandoned.

The second policy dilemma, Ortiz said, concerned the proper role of fiscal policy. In a few cases, notably Russia (1998) and Argentina (2000–01), there was a direct case for fiscal consolidation (defined as periods of sharp deficit reductions) given the contribution of public finance problems to the crisis. However, in crisis countries where the government finances were in better shape, the case for fiscal consolidation was more indirect. The initial programs did provide for fiscal consolidation to make room for emergency spending and to help rebuild confidence among creditors. However, a policy of fiscal consolidation could damage the prospects of a recovery and fuel social discontent, ultimately damaging the confidence of foreign investors—exactly the opposite of what is intended. In response to these considerations, many programs were redesigned: social spending was protected and the fiscal targets were relaxed.

IMF lending dilemma. Typically, IMF assistance is determined on the basis of repayment capacity and balance of payments need. But the volatility of the exchange rate during capital account crises and the fragility of macroeconomic forecasts make the evaluation of the balance of payments needs especially difficult. Undershooting the critical amount of official support will not elicit a favorable response from investors, leaving the program underfinanced. In contrast, meeting or overshooting that critical level of support might have the effect of making it unnecessary for the country to use all available official resources. These facts were recognized by the IMF. The size of its packages was unusually large, and the disbursements under these programs were considerably more front-loaded than usual.

Moral hazard. It has been argued that the availability of IMF financing promotes irresponsible behavior among investors. This concern has been at the top of the list of concerns of IMF officials, supporters, and critics since the Mexican rescue package of 1994, which set a new precedent for official support. But *did* these large bailouts create moral hazard?

According to Ortiz, there is no evidence that global investors count on bailouts and invest regardless of risk. Quite the contrary. In the period following the Mexican crisis, for example, the dispersion of sovereign bond spreads across countries was significantly higher, suggesting that investors are becoming increasingly sensitive to the particular prospects of different countries. This is confirmed by the finding that the sensitivity of sovereign spreads to changes in credit ratings increased after the Mexican crisis, contrary to what the moral hazard hypothesis implies.

There is no evidence that global investors count on bailouts and invest regardless of risk.
—Guillermo Ortiz

Crisis prevention

Domestic policies. Sound monetary and fiscal policies, Ortiz said, are necessary but not sufficient conditions to avoid a capital account crisis. A slight change in policies can lead to a significant deterioration in the perception of a country's prospects. The lessons from the recent balance of payments crises have led countries to pursue a number of additional policy adjustments, including

- following a proactive debt policy and increasing international reserves;
- reinforcing regulation and supervision of the financial sector;
- giving incentives to limit private indebtedness, such as a flexible foreign exchange regime;
- increasing transparency by publishing timely information as well as establishing channels of communication with the private sector; and
- undertaking institutional reform—such as establishing an independent central bank and adopting standards and codes—to increase certainty for the private sector.

Implications for the international financial architecture. In liquidity crises, where the necessary policy adjustment is small, a fast response mechanism—such as the IMF's Contingent Credit Line (CCL)—is needed. The CCL mechanism allows countries to prequalify on the basis of their economic policies and macroeconomic situation. In addition, its size is larger than a typical IMF program and its disbursement faster. However, Ortiz warned that the CCL has four main problems:

- It can be used only for contagion problems.
- It needs an exit strategy for those countries that lose access to the CCL.
- The commitment fee should be reduced.
- The one-year maturity should be increased.

The CCL should therefore be complemented with private sector involvement. One option is to establish contingent credit lines with private banks. Another one is to include options in bonds that would allow for a late repayment under certain conditions.

For most balance of payments crises, Ortiz noted, the problem will remain between clear-cut liquidity and solvency crises. IMF-supported programs have been successful in helping many of the countries that suffered crises in the 1990s to recover macroeconomic stability and return to capital markets in a relatively short time. However, potentially larger flows imply that the depth of the resulting crises could be even larger in these cases. Therefore, countries need larger and more front-loaded IMF packages. As in liquidity crises, mechanisms also need to be developed that would allow for private sector involvement.

How can one tell if a country is experiencing a solvency crisis that warrants a partial default and a subsequent renegotiation process? In practice, this is very difficult. According to Ortiz, in those circumstances in which the debt sustainability criteria do not give a clear indication of insolvency, countries in trouble should initially be given the benefit of the doubt because it is more costly to treat a liquidity problem as a solvency one than to treat a solvency crisis as a liquidity crisis.

Two proposals have been put on the table in cases where it is unlikely that the renegotiations will be orderly and consensual. The first is to include collective action clauses in bonds, but, Ortiz noted, this has significant problems in practice. The other proposal is for the IMF to establish a procedure for debt standstills where a qualified majority of creditors would be sufficient to accord the debtor relief from legal action. This second option—for a sovereign debt restructuring mechanism—is a better solution but also has its problems: the IMF, for instance, would still need to validate whether the country can use the procedure. An alternative is to give the three parties to the renegotiation—the IMF, the sovereign, and the investors—proper incentives. The IMF, for example, could provide certain financing at a minimum haircut—a mandatory loss imposed on creditors—and after that, it could support increases in the size of the haircut.

Conclusion

Because of the significant problems that international financial markets face from the extreme volatility in emerging markets, Ortiz stressed that there is an important leadership role for the international financial institutions and the Group of Seven governments to play to make the transition toward the new architecture a smooth one. If the international community fails in this attempt, he concluded, it runs the risk of shutting emerging markets out of international financial markets and generating a political backlash against trade and financial integration in developing countries. ■

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It is more costly to treat a liquidity problem as a solvency one than to treat a solvency crisis as a liquidity crisis.
—Guillermo Ortiz

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Caribbean centers

Stricter rules change climate for offshore financial centers

In recent years, many English-speaking Caribbean countries have looked for new ways to diversify their economies and stimulate economic growth. Developing the service sector, especially offshore financial activities, may seem an attractive way to diversify, and proponents point to such success stories as The Bahamas and the Cayman Islands. But a new IMF Working Paper, Caribbean Offshore Financial Centers: Past, Present, and Possibilities for the Future, *by Esther C. Suss, Oral H. Williams, and Chandima Mendis, urges caution, since a new and more stringent regulatory environment may make it difficult for the region's new offshore financial centers to gain a firm foothold.*

The English-speaking Caribbean countries face a particular set of challenges. Their small, open economies have long been vulnerable to external shocks. In the past, many of these islands depended heavily on agriculture—often specializing in one main export, such as bananas or sugarcane. Preferential trade agreements with the European Union helped maintain the profitability of these exports, but these arrangements are now considered a violation of World Trade Organization rules, with likely significant adverse effects for employment and external current account balances.

In the search for higher growth, a number of countries have pursued expanded tourism, but here, too, there have been shortcomings. The sector's highly competitive nature and the region's vulnerability to hurricanes have limited the gains that can be reaped from this sector.

The offshore financial center option

In looking for other areas in which to diversify, more island economies began to consider developing offshore financial centers. This sector is particularly appealing because it does not require a large skilled workforce or major investment in infrastructure.

The sector has a long history in the region. The Caribbean's first offshore operations were established in The Bahamas in 1936 and, shortly thereafter, in Anguilla, the British Virgin Islands, and the Cayman Islands. Their success inspired other Caribbean nations, such as Antigua and Barbuda, Dominica, Grenada, Nevis, St. Kitts, St. Lucia, and St. Vincent and the Grenadines, to enter the sector—some as recently as the late 1990s.

The older offshore financial centers developed slowly over time, and their economies reaped long-term benefits in the form of a more highly skilled workforce; improved infrastructure; better services, such as hotels, restaurants, and catering; and, more generally, additional foreign investment in their economies. Some older offshore centers, such as the Cayman Islands, now have a large and diverse international financial sector.

If a country acquires a reputation—rightly or wrongly—as a haven for criminal activities, then onshore banks will not want to be associated with them and the offshore sector will not thrive.

What do offshore financial centers do?

Offshore financial centers provide financial management services to foreign users in exchange for foreign exchange earnings. The comparative advantage for clients? Several, including very low tax rates, minimal administrative formalities, and confidentiality and discretion. This environment allows wealthy international clients to minimize potential tax liability while protecting income and assets from political, fiscal, and legal risks. There are many vehicles through which offshore financial services can be provided. These include the following:

- *Offshore banking*, which can handle foreign exchange operations for corporations or banks. These operations are not subject to either capital, corporate, capital gains, dividend, or interest taxes or to exchange controls.
- *International business corporations*, which are often tax-exempt, limited-liability companies used to operate businesses or raise capital through issuing shares, bonds, or other instruments.
- *Offshore insurance companies*, which are established to minimize taxes and manage risk. Onshore insurance companies establish offshore companies to reinsure certain risks and reduce their reserve and capital requirements.
- *Asset management and protection* allows individuals and corporations in countries with fragile banking systems or unstable political regimes to keep assets offshore to protect against the collapse of domestic currencies and banks. Individuals who face unlimited liability at home may use offshore centers to protect assets from domestic lawsuits.
- *Tax planning.* Multinationals may route transactions through offshore centers to minimize taxes through transfer pricing. Individuals can make use of favorable tax regimes offered by offshore centers through trusts and foundations.

The tax concessions and secrecy afforded by offshore financial centers can be used for many legitimate purposes, but they have also been used for illegitimate ends, including money laundering and tax evasion.

But can their success be replicated by the new offshore financial centers in the region? In a review of the Caribbean's experience, the authors find solid evidence of the benefits that have accrued to the economies of established centers but doubt whether the newer centers will find it cost-effective to operate in a more stringent, and initially more costly, regulatory environment.

New regulatory climate

The volume of flows into offshore financial centers, concerns about money laundering, and links to illegal and terrorist activity (heightened after September 11) have translated over the past few years into increased calls to better regulate and supervise offshore financial operations. Various international committees, such as the Financial Action Task Force (FATF) and the Financial Stability Forum (FSF), have drawn up best-practice guidelines for offshore financial centers. These new guidelines aim at making offshore centers' operations more transparent, and sanctions have been proposed for centers that do not meet international standards.

Compliance with these higher standards has posed particular issues for some of the newer entrants to the offshore financial sector. Many of these nascent centers had sought to offer broad banking secrecy as one way of luring business away from the older offshore financial centers. Now these new entrants will not only lose this means of differentiating themselves from their more established competitors, but will also incur additional expenses to comply with the new rules, which entail establishing a series of regulatory institutions and hiring independent auditors to oversee their activities.

The FSF and FATF reports list "uncooperative" countries—countries that are judged to fall short of meeting, or of moving toward meeting, international standards—and these reports bring adverse publicity to offshore operations. Since reputation is key in this business, being cited as uncooperative can compromise the development of the whole financial sector in these countries. If a country acquires a reputation—rightly or wrongly—as a haven for criminal activities, then onshore banks will not want to be associated with them and the offshore sector will not thrive.

Cost-effective?

According to the authors, the well-established offshore financial centers, which had developed unfettered by intense international scrutiny, are not likely to be greatly affected by the cost of complying with international standards. These centers have already reaped many of the benefits associated with this sector and often have the required institutions already in place.

Offshore financial centers that began operating in the 1990s, however, may find themselves in a more difficult position. They must establish their operations in the glare of the international spotlight, and, at least over the short run, they must absorb the cost of complying with international standards—costs that may nearly equal the revenues gained from offshore financial activities.

The authors conclude with a word of caution. Countries with nascent offshore financial centers may not find these operations profitable in the newly stringent regulatory environment. They are urged to conduct a careful cost-benefit analysis before devoting more resources to developing this sector. The authors also counsel that the in-depth analyses that are needed will require that national authorities obtain and share necessary data and pursue greater openness—all steps that may not be easily accomplished in a sector that has traditionally operated in the shadows. ■

Offshore financial centers can provide significant government revenues
(percent of GDP)

	Total revenues[1]						Costs[2]	Net revenue
	1995	1996	1997	1998	1999	2000	2000	2000
ECCU area[3]								
Anguilla	…	…	0.9	0.8	0.8	0.8	0.3	0.5
Antigua and Barbuda	0.3	0.3	0.8	0.7	1.3	1.3	0.2	1.1
Dominica	0.0	0.7	1.6	1.5	1.4	0.7	0.3	0.4
Grenada	…	…	…	…	1.0	1.2	0.4	0.8
St. Kitts and Nevis	0.3	0.4	0.5	0.7	0.8	0.8	0.2	0.6
St. Vincent and the Grenadines	…	…	0.2	0.3	0.4	0.4	0.5	0.0
Rest of the Caribbean								
The Bahamas	0.3	0.2	0.2	0.2	0.2	0.2	0.0	0.2
Barbados	0.1	0.2	0.4	0.4	0.4	0.7	0.1	0.6
British Virgin Islands	9.9	10.7	11.5	12.1	12.3	13.1	0.3	12.8
Cayman Islands	3.0	3.1	3.1	3.4	4.2	4.1	0.2	3.9

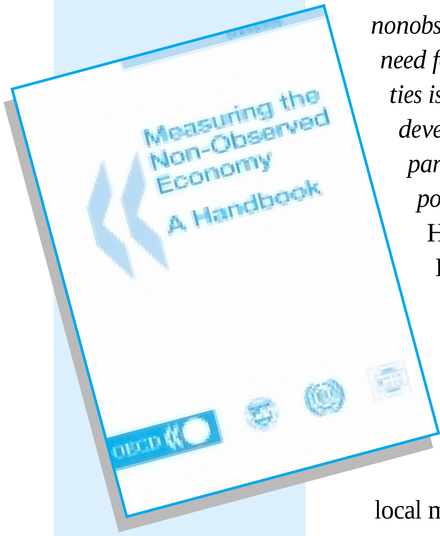
[1]Consists mainly of licensing and registration fees.
[2]IMF staff estimates using data from national authorities.
[3]Eastern Caribbean Currency Union area.
Data: International Financial Sector Authority, Antigua and Barbuda; Ministry of Finance, Dominica; Nevis Financial Services Department; KPMG, Review of Financial Regulation in Caribbean Overseas Territories and Bermuda, October 2000; Offshore Financial Authority, St. Vincent and the Grenadines; and IMF staff estimates.

Copies of IMF Working Paper No. 02/88, *Caribbean Offshore Centers: Past, Present, and Possibilities for the Future*, by Esther C. Suss, Oral H. Williams, and Chandima Mendis, are available for $10.00 each from IMF Publications Services. See page 251 for ordering details.

Many of these nascent centers had sought to offer broad banking secrecy as one way of luring business away from the older offshore financial centers.

New Handbook

Statisticians tackle task of measuring shadows



Unmeasured and underground economic activities thrive to some degree in all countries—rich and poor. How extensive are they? What role do they play in national economies? Probing the size and impact of nonobserved economies is a daunting task. But the need for more accurate measurement of these activities is increasingly evident, particularly in the developing and transition countries, where the parallel economy often accounts for a significant portion of total production. The newly issued Handbook on Measuring the Non-Observed Economy *offers a compendium of good practices and a strategy for compiling more comprehensive data about shadow economies.*

In a rural Punjabi village, a man, his wife, his in-laws, and his children cut and stitch sandals that they will sell in the local marketplace. In Washington, D.C., an entrepreneur employs illegal aliens to provide lawn care and gardening services in the upscale suburbs of the capital. A young mother in Malawi tends a small plot of vegetables to supplement her family's meager diet. A continent away, an adolescent is sent to work for a prostitution ring in a neighboring country. Disparate though these activities may be, they have one thing in common: the goods and services they produce make up part of the nonobserved economies of their countries.

Estimating the unmeasured

Governments, policymakers, and researchers have long puzzled over how to measure economic activity in informal and household sectors as well as underground and illegal activities. National accounts, deprived of data on these often significant economic activities, do not accurately measure GDP, poverty, income, and other variables on which data are necessary for the formulation of effective economic and social policies. Missing data can significantly undermine the accuracy of a country's official statistics. Inaccurate statistics may impair the effectiveness of adjustment programs that countries devise with the IMF and other multilateral institutions, since these programs rely heavily on GDP figures.

To date, various attempts to estimate this missing production have proved largely ineffective. Monetary models have been used to estimate changes in missing economic activities on the basis of changes in the patterns of currency demand. Other models have been used to provide estimates on the basis of changes in electricity consump-

East Timor joins the IMF

East Timor's Prime Minister, Mari Alkatiri (left), is welcomed to the IMF by Managing Director Horst Köhler.

The Democratic Republic of East Timor become the 184th member of the IMF on July 23, when the Prime Minister, His Excellency Mari Alkatiri, signed the IMF's Articles of Agreement in Washington, D.C. The country's initial quota in the IMF is SDR 8.2 million (about $11 million). With the admission of East Timor, the total of members' quotas is SDR 212.6 billion (about $285 billion).

Welcoming East Timor's membership on July 24, IMF Managing Director Horst Köhler noted that the country was claiming its place as a respected member of the global community and demonstrating its commitment to meeting the responsibilities and reaping the benefits of international cooperation.

Economic activity has recovered in East Timor "since the violence and devastation of late 1999," Köhler said, noting the contributions of many, but particularly the East Timorese, to this recovery. "While the international community has helped," he said, "these achievements are, fundamentally, a tribute to the endurance of the East Timorese people and to the commitment of your leadership in establishing the foundations of a stable and prosperous future."

East Timor is one of the world's poorest countries, and it faces many challenges. "While those challenges are significant, Köhler indicated that he is "confident that, with the continued support of the international community and your commitment to setting the country on a sound policy path, East Timor will rise to the occasion, as it has done so many times in the past."

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tion. All such models, however, rely on overly simple assumptions.

Good practices

If earlier efforts proved to be inadequate, is there scope now for a more comprehensive and sustained effort? The experience of the IMF Statistics Department, gained through technical assistance and training efforts in a variety of countries, clearly indicates that there is. Building upon this experience, Adriaan Bloem and Manik Shrestha describe in IMF Working Paper No. 00/204, *Comprehensive Measures of GDP and the Unrecorded Economy*, how a more comprehensive and accurate measurement may be achieved.

This working paper served as a cornerstone for the *Handbook*, which was produced jointly by the Organization for Economic Cooperation and Development (OECD), the IMF, the International Labor Organization, and the Interstate Statistical Committee of the Commonwealth of Independent States and is designed to assemble best practices and promote their adoption.

Based on the *System of National Accounts 1993*, which provides an international standard for the measurement of GDP, the *Handbook* elaborates a measurement strategy for the nonobserved economy that is applicable in all countries, regardless of whether a statistical system is advanced, developing, or in transition. This measurement strategy is based on five main components:

- identifying an appropriate conceptual and analytical framework on which the nonobserved economy can be assessed;

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"Crisis Prevention and Resolution: Lessons from Argentina,"Anne Krueger, IMF First Deputy Managing Director, National Bureau of Economic Research (NBER) Conference, Cambridge, Massachusetts, July 17 (see page 241)

"The U.S. and Japan in the Global Economic System," Shigemitsu Sugisaki, IMF Deputy Managing Director, Twentieth Anniversary of the CSIS Japan Chair, Washington, D.C., July 24

"Preventing and Resolving Financial Crises: The Role of Sovereign Debt Restructuring," Anne Krueger, IMF First Deputy Managing Director, Sao Paolo, Brazil, July 26

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- assessing the basic data being supplied for the national accounts and the compilation methods used, identifying the extent of nonobserved and nonmeasured activities, and establishing priorities for dealing with them in the immediate future and over the longer term;
- identifying potential improvements in how the national accounts are compiled. Such improvements would seek to reduce the amount of nonmeasured activities by incorporating model-based adjustments and the results of supplementary surveys;
- strengthening the infrastructure and content of the basic data collection program by bringing the program into line with international standards and best practices; and
- developing an implementation plan that includes consulting with users, prioritizing the potential improvements, ensuring good communication between survey statisticians and national accountants, and dealing with revisions to national accounts estimates that may occur as a consequence of the changes.

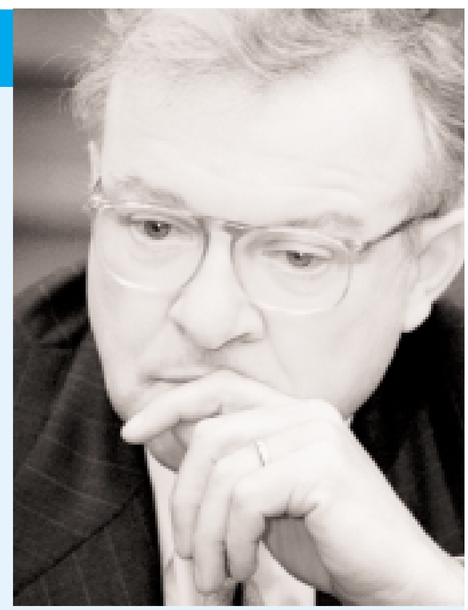
In addition, the *Handbook* provides examples of analytical frameworks that can be used to assess the magnitude and nature of nonobserved activities and suggests supplementary surveys that may provide additional information. It includes advice on how to formulate stand-alone statistics for the informal sector and for household production undertaken for own final use, such as the growing of food for personal consumption. It also offers other useful suggestions, such as how to tailor a measurement plan to the particular circumstances of a country. For country economists, the most useful information may well be the tips and shortcuts the *Handbook* offers on estimating activities within the shadow economy where good data are not available.

The *Handbook* is chiefly intended for those who produce and use macroeconomic statistics, but its detailed information on the nature and the dimensions of informal and underground economies may also be of interest to researchers, journalists, and others seeking to learn more about an aspect of national economies that in quantitative terms had long remained a mystery. ■

Gail Berre
IMF External Relations Department

Copies of *Measuring the Non-Observed Economy: A Handbook* are available for $50.00 each from IMF Publications Services. For ordering details, see page 251.

Rudiger Dornbusch remembered



On July 25, MIT professor Rudiger Dornbusch died of cancer at the age of 60. Dornbusch, who was born in Germany and studied at the universities of Geneva and Chicago, taught at MIT for more than a quarter century and coauthored, with Stanley Fischer, a textbook—*Macroeconomics*—that is standard fare for undergraduate and graduate studies.

In paying tribute to Dornbusch, IMF Managing Director Horst Köhler said "It is with great sadness that we must accept the passing of Professor Rudiger Dornbusch, one of the great economists of our day. His research has had a profound impact on our work at the IMF; he leaves behind a rich legacy of ideas. Fortunately, he has also left behind a great many of his students, no small number of whom are here working at the IMF. Rudiger Dornbusch was a man of enormous charm, humor, and wit—one of those people who is larger than life. We shall miss him greatly."

Kenneth Rogoff, the IMF's Economic Counsellor and Director of the Research Department, noted "With the passing of Professor Rudi Dornbusch, we have all—in the economics profession and particularly at the IMF—suffered an incalculable loss. To simply say that he was one of the great economists of our time is not enough. His justly celebrated 'overshooting' paper is, indeed, arguably the most influential article written in the field of international economics since World War II. His policy ideas on how to better manage debt crises had a crispness and originality unlike any other's.

But what his many students and followers throughout the world loved most was Dornbusch the man, full of vitality, creativity, sharpness, humor, and deep personal warmth. As a path-breaking scholar, as a beloved teacher, and as a cogent policy advisor to many countries, Rudiger Dornbusch lived one of the great lives in economics."

For a recent tribute by Kenneth Rogoff to Rudiger Dornbusch, see *Dornbusch's Overshooting Model After Twenty-Five Years* (www.imf.org/external/pubs/cat/longres.cfm?sk=15653.0). A recent interview with Professor Dornbusch appeared in the March 25 issue of the *IMF Survey*, pp. 93–96 (www.imf.org/external/pubs/ft/survey/2002/032502.pdf#page=13).