

IN THIS ISSUE

- 82 What's on
- 82 IMF financial data
- 83 In the news
 - De Rato meets with African leaders*
- 84 Country briefs
 - Belgium, Ecuador, Finland, Nepal*
- 86 Country focus
 - U.K. policy frameworks*
 - Fiscal sustainability in Ghana*
- 90 Regional focus
 - Africa in the Doha Round*
- 92 Research
 - Euro area product markets*
 - FDI to Asia*
- 95 IMF lending
 - Arrangements*
- 96 Policy
 - Assessing financial stability*

De Rato urges Africa to harness increased aid flows

page 83

The IMF expects GDP growth in sub-Saharan Africa to exceed 5 percent in 2006 for the third straight year, Rodrigo de Rato told a news conference in Lusaka during a March 13-17 visit to Zambia and Equatorial Guinea. But growth will need to be higher for Africa to meet the Millennium Development Goals. In Bata to address a regional summit, he also urged leaders to tackle corruption and ensure effective use of increased aid.



Richard Ukw/IMF

Lessons from U.K. policy frameworks

page 86

Over the past decade, average per capita growth in the United Kingdom has been more robust and less variable than in any other Group of Seven country. Many factors have been at play, but clearly the country's strong and transparent frameworks for monetary and fiscal policy and sound implementation have made an important contribution. There may be lessons here for other countries, say the IMF's Susan Schadler and James Morsink.



Steve Allen/PictureArts

Africa in the Doha Round

page 90

Africa's two key objectives in the World Trade Organization's current Doha Round of trade negotiations have been to increase access to industrial country markets and continue to benefit from preferential treatment. A new IMF Policy Discussion Paper argues, however, that African negotiators should not overlook the potential market access gains in developing countries, where trade barriers remain relatively high and demand for African imports has expanded substantially over the past decades.

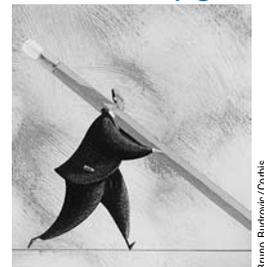


Seylou/AP/Getty Images

Safeguarding financial stability

page 96

Financial stability can be difficult to measure and monitor, but a new book by the IMF's Garry Schinasi seeks to remedy that situation. *Safeguarding Financial Stability: Theory and Practice* lays out a comprehensive approach for assessing the sources of risk and vulnerability in national and international financial systems. The approach, based on analysis of macroeconomic and financial conditions and of institutions, markets, and infrastructures, can be adapted to countries' needs.



Bruno Budrovic/Corbis

What's on

MARCH

29 IMF Book Forum, "Is Globalization Here to Stay?" with Jeffrey Frieden, author of *Global Capitalism: Its Fall and Rise in the Twentieth Century*, Washington, D.C., United States

APRIL

3–5 Inter-American Development Bank Annual Meeting, Belo Horizonte, Brazil

4–6 Seventh International Scientific Conference, "Modernization of Economy and the State," State University–Higher School of Economics, with World Bank and IMF participation, Moscow, Russia

5–6 World Economic Forum on Latin America, São Paulo, Brazil

22–23 IMF–World Bank Spring Meetings, Washington, D.C., United States

24 United Nations Economic and Social Council High-Level Meeting with the IMF, World Bank, World Trade Organization, and United Nations Conference on Trade and Development, New York, United States

MAY

3–6 Asian Development Bank Annual Meeting, Hyderabad, India

20–22 World Economic Forum on the Middle East, "Embracing the Future: Unleashing the

Potential of the Middle East," Sharm El-Sheikh, Egypt

21–22 European Bank for Reconstruction and Development Annual Meeting and Business Forum, London, United Kingdom

22–23 Organization for Economic Cooperation and Development Forum 2006, "Balancing Globalization," Paris, France

22–27 World Health Assembly, World Health Organization, Geneva, Switzerland

29–30 World Bank, Annual Bank Conference on Development Economics, Tokyo, Japan

31–June 2 World Economic Forum on Africa, "Going for Growth," Cape Town, South Africa

JUNE

15–16 World Economic Forum on East Asia, "Creating a New Agenda for Asian Integration," Tokyo, Japan

19–23 World Urban Forum III, Vancouver, Canada

JULY

15–17 Group of Eight summit, St. Petersburg, Russia

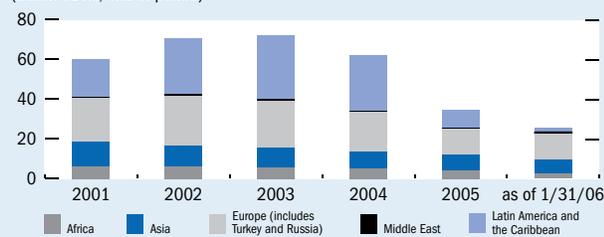
IMF Executive Board

For an up-to-date listing of IMF Executive Board meetings, see www.imf.org/external/np/sec/bc/eng/index.asp.

IMF financial data

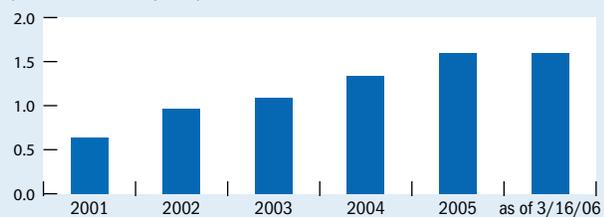
Total IMF credit and loans outstanding, by region

(billion SDRs, end of period)



HIPC debt relief¹

(billion SDRs, end of period)



¹Cumulative disbursements under the Heavily Indebted Poor Countries Initiative.

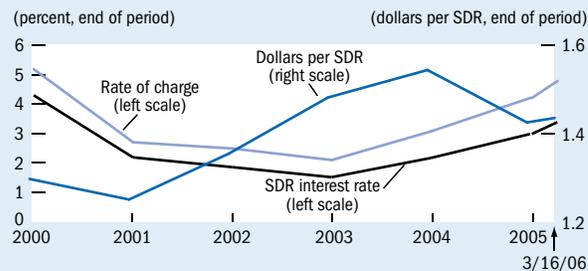
Note: Special Drawing Rights (SDRs) are an international reserve asset, created by the IMF in 1969 to supplement the existing official reserves of member countries. SDRs are allocated to member countries in proportion to their IMF quotas. The SDR also

Major currencies, rates per SDR

	March 17, 2006	Year ago (March 17, 2005)
Euro	1.189	1.150
Japanese yen	169.009	160.454
U.K. pound	0.825	0.799
U.S. dollar	1.448	1.533

Related rates

SDR interest rate, rate of charge on IMF nonconcessional loans outstanding, and dollars per SDR



serves as the unit of account of the IMF and some other international organizations. Its value is based on a basket of key international currencies.

De Rato urges Africa to tackle corruption, build on debt write-off

The IMF expects sub-Saharan Africa's GDP to grow by 5.4 percent in 2006, the third straight year of growth above the 5 percent level, Managing Director Rodrigo de Rato told a news conference in Lusaka, Zambia, on March 16. But he warned that growth needs to be even higher if Africa is to meet the Millennium Development Goals (MDGs) and urged African leaders to ensure that increased aid flows were used effectively.

De Rato was on his fourth visit to sub-Saharan Africa as Managing Director of the IMF and his first since the IMF agreed to write off 100 percent of the debt owed to it by 19 highly indebted poor countries—13 in sub-Saharan Africa.

Speaking at a roundtable in Lusaka of finance ministers, parliamentarians, civil society leaders, and journalists from Ethiopia, Ghana, Malawi, Mozambique, Tanzania, Uganda, and Zambia, de Rato highlighted the renewed commitment by the international community to increase aid significantly to help low-income countries achieve the MDGs. But he stressed that African governments must draw up policy frameworks that allow resource flows to reach their targets, especially education and health—including measures to counter the HIV/AIDS pandemic. And he discussed ways in which the IMF could help African countries under its new medium-term strategy, including advising on how to tackle problems associated with scaled-up aid flows. De Rato underscored that African countries and the international community must make sure that the forgiven debt is not quickly replaced with new debts, possibly on worse terms.

De Rato met with Zambian President Levy Mwanawasa, Finance Minister Ng'andu Magande, and other members of the Zambian economic team. "Zambia has pursued a strategy of promoting macroeconomic stability and good public sector management and encouraging sound growth of the financial and private sectors," de Rato told the press at the conclusion of his visit. "We at the IMF have been glad to support these efforts."

Before arriving in Zambia, de Rato delivered the keynote speech at the summit of the Economic and Monetary Community of Central Africa (CEMAC) in Equatorial Guinea on March 15. He said this was a propitious time for Africa to make a strong push for both economic reform and improved



Rodrigo de Rato meets with President Teodoro Obiang Nguema Mbasogo of Equatorial Guinea (top photo) and Zambian President Levy Mwanawasa (bottom photo).

trade by reducing tariffs. But de Rato, a former Spanish Economy Minister, called for increased transparency and public accountability in African oil-producing countries that have received a windfall from recent higher oil prices. Five of the six CEMAC members are oil exporters.

"Corruption is an issue that must be dealt with," he declared, arguing that it was important to ensure that oil revenues were spent wisely. "There are many people who have not benefited from this windfall," said de Rato, pointing to the poor social indicators in CEMAC countries. The Managing Director met with the Presidents of Equatorial Guinea, the Central African Republic, the Republic of Congo, Gabon, and São Tomé and Príncipe. He also signed a service agreement with President Obiang of Equatorial Guinea for a two-year technical assistance project that will begin shortly.

In addition to his official meetings, the Managing Director visited facilities for orphans in Equatorial Guinea and in Zambia. He made donations of \$5,000 to each of the orphanages on behalf of the Fund. ■

IMF establishes new AFRITAC

The IMF announced that it will establish the third African Regional Technical Assistance Center (AFRITAC) to serve the CEMAC member countries (Cameroon, Chad, Central African Republic, Republic of Congo, Equatorial Guinea, and Gabon), as well as Burundi and the Democratic Republic of Congo. The center, which will be located in Libreville, Gabon, is expected to begin operations by January 2007.

Belgium should boost employment and restrain public spending

Growth in Belgium picked up during 2005, from 0 percent in the first quarter to 2.5 percent (at an annual rate) in the fourth, owing to stronger growth of exports and household consumption. According to the IMF's annual economic review, annual growth should strengthen to slightly above 2 percent in 2006 from 1.5 percent in 2005 as demand from trading partners continues to increase, private consumption improves in response to tax cuts, and residential construction remains resilient. Inflationary pressures are also growing, however, because of higher wages and oil prices.

As elsewhere in Europe, population aging is weighing on the budget and on growth, while employment is significantly lower than the EU15 average. With a balanced budget since 2000, public debt has fallen as a share of GDP, allowing the government to fund the costs of aging through interest savings. The authorities are implementing the Generation Pact, designed to increase jobs for young, low-skilled, and older workers. Since 2004, the financial sector has been strong and profitable.

The IMF Executive Board applauded the economy's continued good performance and was optimistic about the near-term outlook and growth projections. Urging the authorities to curb medium-term spending, Directors advised adding a comprehensive approach to tax reform to efforts to reduce public debt and support growth and discouraged using tax amnesties and ad hoc

Belgium	2002	2003	2004	Est. 2005 ¹	Proj. 2006 ¹
Real GDP (percent change)	1.5	0.9	2.4	1.5	2.1
Unemployment rate (percent of labor force)	7.3	8.0	7.9	8.3	8.2
General government balance (percent of GDP)	0.0	0.1	0.0	0.0	-0.4
General government debt (percent of GDP)	103.2	98.5	94.9	94.0	90.4

¹IMF staff estimates and projections.

Data: Belgian authorities and IMF staff estimates.

tax measures to meet revenue objectives. The authorities were praised for meeting budget targets and for their intention to use revenue from higher growth to balance the 2006 budget.

While welcoming the Generation Pact, Directors noted that measures should be extended to phase out early retirement regimes and improve the employability of older workers. Wage moderation is essential to preserve competitiveness and promote job creation, they said, and indexation should be abandoned. The Financial System Stability Assessment was well received, particularly the view that the financial sector is stable and resilient. Directors underscored the need to maintain high-quality banking supervision and to raise the quality of insurance and pension fund supervision to the same level. Maintaining adequate oversight of the settlement systems is essential. ■

Stronger public finances, structural reforms are key to Ecuador's growth

Despite a difficult political environment, Ecuador recorded a generally positive economic performance in 2005, the IMF said in its economic review. The strong growth in the oil sector that followed the completion of a pipeline in 2003 has tapered off, but high oil prices have helped underpin domestic demand. Employment growth remained sluggish, however, and inflation picked up in the second half of 2005 in the context of significant increases in bank credit and public spending. In addition, while banking intermediation grew strongly, it is still well below pre-crisis (1997) levels, and the overwhelming majority of deposits are at short maturities.

The IMF Executive Board expressed particular concern about the widening non-oil fiscal deficit. While welcoming the authorities' plan to strengthen the fiscal policy stance in 2006, Directors stressed the need for a solid institutional framework for promot-

ing fiscal discipline, reduced dependence on oil revenue, greater budget flexibility, and higher-quality government spending. They also urged the authorities to follow through on reforming the tax system and emphasized the need to control civil service wage costs, reform the pension system, reduce highly distortional fuel subsidies, and strengthen the social safety net to help those most vulnerable to subsidy cuts.

Directors welcomed ongoing efforts to improve financial sector supervision and regulation. At the same time, they underscored the need for an effective deposit insurance system and an adequate lender-of-last-resort facility. Outstanding issues from the 1998-99 banking crisis, particularly the liquidation of the remaining closed banks and the return of frozen deposits, must also be resolved. Directors expressed grave concerns about provisions in the banking reform bill that would introduce administrative controls on interest rate spreads and credit allocation because such provisions could stifle the much-needed expansion of financial intermediation and jeopardize banking system stability.

To sustain competitiveness and allow the economy to reap the full benefits of dollarization, Directors called for intensified structural reforms. To attract private investment, high priority should also be given to developing the petroleum sector, including through a comprehensive reform of PetroEcuador; strengthening the petroleum sector's regulatory framework; and setting market-based prices for oil products. ■

Ecuador	2002	2003	2004	Projections	
				2005	2006
	(annual percent change, unless otherwise indicated)				
Real GDP	3.4	2.7	6.9	3.2	2.7
Consumer price index, end of period	9.4	6.1	1.9	4.3 ¹	3.0
Credit to the private sector	13.6	4.5	28.6	26.2 ¹	11.6
Noninterest expenditure (percent of GDP)	21.5	20.7	22.0	23.8	23.7
Overall fiscal balance (percent of GDP)	1.0	1.7	2.3	1.7	2.2

¹Actual.

Data: Central Bank of Ecuador; Ministry of Finance; and IMF staff estimates and projections.

Finland's continued economic success rests on strengthened fiscal position

In recent years, Finland's economy has performed favorably. Growth, which has outpaced that in the euro area, is expected to surpass 3 percent in 2006; the external current account has remained in surplus; and inflation has remained below the euro area average, thanks to strong productivity growth and wage moderation, increased domestic competition, and low nonfuel import prices. Public finances are in surplus but have weakened because of personal income tax cuts and growing local government expenditures. This weakening, along with the imminent rise in old-age dependency, is clouding the long-term outlook for growth and fiscal sustainability, the IMF said in its annual review.

The IMF Executive Board commended the authorities for Finland's strong economic performance and stressed the need to strengthen the fiscal position and continue to implement reforms to cope with the challenges of an aging population. While welcoming recent tax cuts, Directors called for further spending restraint. They also welcomed the authorities' efforts to reorganize the provision and financing of public services and suggested measures to limit demand, including more effective implementation of user charges. Directors also welcomed pension reforms being phased in and called for further measures to enhance long-term sustainability.

Nepal's economy remains stable despite security problems

Political turmoil and conflict in Nepal reduced growth in 2005, but, according to the IMF's annual economic review, inflation was moderate, the overall fiscal deficit was significantly lower than budgeted, the current account and overall balance of payments remained in surplus, and international reserves were adequate. Financial soundness indicators also improved somewhat, thanks to banking sector reforms.

The IMF's Executive Board commended the authorities for maintaining macroeconomic stability in a difficult environment but noted that the country is at a critical juncture, as political uncertainties and the ongoing insurgency continue to dampen economic growth. Executive Directors encouraged the authori-

Finland	2003	2004	2005 ¹	2006 ¹
GDP (percent change)	2.4	3.6	1.9	3.5
Harmonized consumer price index (percent change) ²	1.3	0.1	0.9	1.5
Overall general government balance (percent of GDP)	2.3	1.9	1.8	1.8
Total domestic credit (percent change) ³	7.7	8.8	14.5	...
Current account balance (percent of GDP)	4.0	4.0	2.8	3.2

¹IMF staff estimates and projections, unless otherwise indicated.
²Consistent with Eurostat methodology.
³For 2005, 12-month increase to October.
 Data: Finnish authorities; IMF, *International Financial Statistics*, and staff estimates.

Employment growth picked up in 2005 after three slow years, but continued efforts will be needed to address growing job mismatches and risks of labor shortages in some sectors. To allow the wage structure to reflect productivity differentials more fully and promote low-skilled labor, Directors pointed to the need for a more flexible centralized wage-bargaining mechanism. Directors also called for further progress on product market liberalization.

Although Finland's financial system is sound and well supervised, Directors emphasized the need for continued vigilance in light of recent rapid credit growth and heightened competition among lenders, especially in the mortgage sector. ■

ties to address key constraints on growth, maintain macroeconomic stability, and reduce poverty.

Directors welcomed efforts to mobilize revenue, prioritize expenditure, increase social sector spending, and limit domestic budget financing. They encouraged the authorities to improve tax administration further. Directors also emphasized the need to increase fiscal transparency, improve public expenditure management, and address donor concerns about the quality of spending. To these ends, they suggested broader coverage of off-budget activities and more comprehensive reporting of security-related spending.

Directors called on Nepal to improve the legal framework for financial sector activity and to make progress with loan recovery from large, willful defaulters. Given the importance of remittances for Nepal, Directors also urged that steps be taken to reduce transaction costs.

Also recommended were stepped-up measures to reform public enterprises and governance, with greater attention paid to prominent offenders. Liquidation of unviable loss-making enterprises should also proceed decisively. To encourage private sector activity, Directors called for an upgrading of the regulatory framework and more flexible labor markets. Given the importance of agriculture and the high level of rural poverty, they also encouraged the implementation of policies to raise agricultural productivity, including upgrading rural infrastructure to promote market access for agricultural products. ■

Nepal	2001/02	2002/03	2003/04	Est. 2004/05	Proj. 2005/06
Real GDP (percent change)	-0.6	3.4	3.4	2.5	2½-3½
Consumer price index (end of period, percent change from 12 months earlier)	3.5	6.1	2.0	6.6	7-9
Overall deficit (after grants, percent of GDP)	4.3	1.6	1.0	0.9	1.2
Overall balance of payments (million U.S. dollars)	-39	93	235	24	-2.4
Gross official reserves (million U.S. dollars)	1,048	1,178	1,471	1,507	1,551
Months of imports of goods and services	7.0	6.6	8.2	7.6	6.7

Note: Fiscal year begins mid-July.
 Data: Nepalese authorities and IMF staff estimates.

For more information, please refer to IMF Public Information Notices No. 06/22 (Belgium), No. 06/15 (Ecuador), No. 06/10 (Finland), and No. 06/12 (Nepal) on the IMF's website (www.imf.org).

Interview with Susan Schadler and James Morsink U.K. policy frameworks prove their mettle

Rising energy prices and sharply decelerating house prices combined to create a challenging environment for U.K. policymakers in 2005. But the economy, which has recorded strong, steady growth in recent years, is proving resilient. In effect, the stresses of the past year have amounted to the toughest test yet for the country's widely respected monetary and fiscal policy frameworks, say Susan Schadler, Deputy Director of the IMF's European Department, and James Morsink, Division Chief for the United Kingdom. They discuss with the IMF Survey why these frameworks may also provide worthwhile examples for other countries facing similar challenges.

IMF SURVEY: The IMF has praised the U.K.'s framework for monetary and fiscal policy. Are there lessons for other countries?

SCHADLER: Other countries can learn much from the United Kingdom's strong, clear, and transparent policy frameworks, which have made important contributions to its robust and steady performance over the past decade. Particularly in the face of the increase in energy prices and deceleration in house prices in the past year, these frameworks have really proved their mettle.

Monetary policy is formulated in an inflation-targeting framework. The independent Monetary Policy Committee, comprising experts from outside and inside the Bank of England, makes decisions on interest rates with the objective of keeping inflation at the 2 percent target. This framework has produced decisions that seem well considered and consistently appropriate.

The fiscal framework has three pillars: clear fiscal rules—the golden rule over the cycle (requiring the current budget

to be in balance or surplus, on average, over a business cycle) and a limit of 40 percent of GDP on net debt of the public sector—that guide decisions about budgets with a medium-term focus while allowing for policy to be countercyclical; transparency requirements; and a medium-term budgeting framework with multiyear spending allocations.

In recent years, this framework has been tested. Starting in FY2000/01, the government increased investment and current spending to meet concerns about the adequacy of public services. When revenues increased less rapidly than the government had projected, however, the deficit grew. Adjustment measures are now needed to bring the fiscal position back in line with the golden rule over the cycle.

To the credit of the fiscal rules, the need for this adjustment is quite transparent. Performance of fiscal policy can be judged against the rule, and there can be a clear discussion about the size of the required adjustment. The IMF staff has taken the position for several years now that an adjustment is needed. The government has been slower to come to this view, but it now has plans that entail immediate measures—such as increased taxation of North Sea energy production—and, starting in FY2008/09, restraint on the growth of current spending. Whenever there is such back-loaded adjustment focused on spending restraint, it is easy to ask whether and how it will be done. The government, however, has clearly committed itself to spending restraint, and the staff has commended this forward-looking commitment. We believe the fiscal framework will help ensure that the commitment becomes reality.

IMF SURVEY: The U.K. experienced a sharp slowdown in house prices in 2005. Are there lessons here for countries whose housing markets are likely to cool in the future?

MORSINK: There are two important lessons. First, a soft landing is possible. The growth rate of U.K. house prices slowed sharply between mid-2004 and mid-2005, but so far there has been no decline in house prices. This is in sharp contrast to the experience of the early 1990s, when a boom rapidly turned into a bust, with significant declines in nominal U.K. house prices. Second, even though house prices appear to have achieved a soft landing, the growth rate of private consumption slowed sharply. House prices can affect consumption through effects



Susan Schadler (with James Morsink): "Other countries can learn much from the United Kingdom's strong, clear, and transparent policy frameworks."

on the value of household wealth and of the associated collateral that may be used as a basis for borrowing. House prices and consumption may also be positively related because they may both be driven by the same variables, such as expectations of income growth. In an IMF Selected Issues Paper, Dora Iakova found that, in the United Kingdom, a 10 percent decline in housing wealth has, in the past, tended to reduce private consumption by about 0.7 percent. The slowdown in house prices in 2004–05 thus explains much of the decline in private consumption growth.

IMF SURVEY: [Given the U.K.'s good policy frameworks and open economy, why has productivity growth been so disappointing in recent years?](#)

SCHADLER: Productivity growth in the United Kingdom over the past decade has been strong, exceeding the average in other Group of Seven countries. However, there is still a 5–10 percent gap in the level of output per hour. We support the government's strategy of addressing the five main drivers of productivity growth (innovation, enterprise, competition, investment, and skills), including its current focus on regulatory reform.

IMF SURVEY: [Many advanced countries have concerns about the viability of their national pension systems. Do the recommendations of the U.K. Pensions Commission add up to a feasible solution?](#)

MORSINK: In most countries, fiscal sustainability is the key concern. In other words, there are now doubts about whether the promises once made can be kept. The U.K. solved this problem several decades ago by shifting the indexing of key elements of the state pension system from wages to retail prices, which rise more slowly. Because the generosity of its state pension system had already been reduced, fiscal sustainability is not now the key issue. However, a frugal state pension system works only if individuals save enough for their own retirement. Unfortunately, there is growing evidence that many people are not saving enough, and this may force future governments to increase the generosity of the state pension system.

To address this issue, the Pensions Commission recently recommended three things. First, it said that the United Kingdom should create a national defined-contribution pension scheme with automatic enrollment and low operating costs to address the difficulty many people face in making rational long-term saving decisions and the high cost of many privately run pension schemes. Second, it suggested improving incentives to save by reducing the projected spread of means testing in the state pension system. On current policies, means testing will cover about three-fourths of pensioners by 2050, and this is likely to have adverse effects on the incentives for saving. And, third, it urged that the pensionable age be raised to 67 from

65 by 2050 to take account of rising life expectancy. This is important to help pay for the increased generosity of the state pension system. These recommendations are a very good first step in developing a national consensus in the U.K. on how to raise private saving while ensuring fiscal sustainability. They are good ideas that other countries, with similar pension systems, should consider.

IMF SURVEY: [Any thoughts on the U.K.'s future challenges?](#)

SCHADLER: As a highly open and quite flexible economy, the United Kingdom is at the cutting edge of economic policies and developments—whether in the refinement of policy frameworks or ways of dealing with globalization. Exploring and understanding how the United Kingdom copes with general trends and specific shocks influencing all advanced economies will therefore remain the most intriguing aspect of the IMF's annual Article IV consultations with the country. Let me mention a few issues that will be challenges for the years to come and on which we hope to focus our work next year.

First, we want to look at what has been and could be the effect of immigration on potential output, inflation, and, more generally, monetary policy decision making. This year, we briefly examined the United Kingdom's experience as one of three European Union members to fully open its borders to migration from the 10 new members. Our report underscores that additional inflows since May 2004 have been moderate—about ¼ of 1 percent of the working-age population—with few signs of significant displacement of local workers. In fact, inflows may have had the beneficial effect of relieving skill shortages.

How globalization affects the U.K. economy is another issue that we want to focus on. A first and obvious impact is on inflation, where we've seen goods prices—heavily influenced by import prices—increase very little or even fall over the past few years. The questions are, how much is globalization influencing inflation, and could this influence allow greater scope for easing monetary policy without inflationary consequences?

Finally, on the fiscal framework, we will continue to ask whether refinements—particularly of the golden rule over the cycle—are possible. The framework's strengths are that it is concrete—once the cycle is defined, the rule is clearly testable—and that it explicitly allows fiscal policy to play a countercyclical role—the budget can be in surplus in good years but in deficit in weak years and the rule will still be met. But a weakness is its dependence on the definition of the cycle. Particularly toward the end of a cycle, there is much room for reasonable economists to disagree. We will ask whether, once current balance has been restored, a rule with a more forward-looking focus would be a clearer and more binding guide for fiscal policy in a country that, in fact, has very mild cycles. ■

Public sector reform is key to fiscal sustainability in Ghana

Although Ghana began liberalizing its economy in the mid-1980s, the government has retained control of some enterprises that engage in quasi-fiscal activities. These are off-budget activities undertaken by the central bank and some public financial and nonfinancial enterprises. How extensive are these activities, and what are their consequences? A new IMF Working Paper by Mali Chivakul and Robert C. York finds that quasi-fiscal activities have caused serious distortions in energy and water consumption and in the investment decisions of the affected enterprises and the private sector.

After Ghana gained independence in 1957, the government assumed control of most of the economy, and, by the early 1980s, the public sector completely dominated production. Publicly owned enterprises were involved in almost all sectors, including finance and banking, with some serving social objectives (for example, nonmarket energy pricing) and other public policy goals (such as transportation). In 1983, the government introduced reforms—including the divestiture of 200 public enterprises—to liberalize and reduce its involvement in the economy. But at the end of 2005, the government still retained full ownership of 35 nonfinancial enterprises, including some of the largest in Ghana, with total assets valued at more than 60 percent of GDP in 2003.

Identifying quasi-fiscal activities

Quasi-fiscal activities entail a net transfer of public resources to the private sector (households and enterprises) through nonbudget channels. In contrast, explicit taxes, subsidies, and direct expenditures are included in the budget and have equivalent effects. If quasi-fiscal activities are pursued, the IMF's *Manual on Fiscal Transparency* recommends that they be clearly identified and the implications spelled out in the government's financial reports.

For public nonfinancial enterprises, quasi-fiscal activities include the pricing of commercial activities below market or cost recovery; the tolerance of payment arrears, unbilled consumption, or low collection rates on services provided; and barter and in-kind transactions.

For public financial institutions, they include subsidized lending and rescue operations or bailouts; the lack of remuneration on commercial banks' reserve requirements; multiple exchange rates and subsidized exchange rate insurance; and central bank operations to sterilize capital inflows and manage liquidity through open market operations.

Because of their extensive activities, these state-owned enterprises play an important role in Ghana's economy. Their efficiency can help lower the cost of doing business for the private sector, and, if they are profitable, they can reduce pressure on the budget and influence the amount of infrastructure investment that is needed to support economic development. The government intends to make all of the commercially oriented state-owned enterprises financially self-sustaining and expects them to make an appropriate contribution to the budget. But several are operating at a loss, largely because of their involvement in quasi-fiscal activities (see box).

Where the losses are

Recent data suggest that quasi-fiscal activities are prevalent in the Volta River Authority, the Electricity Company of Ghana, the Ghana Water Company Limited, and the Tema Oil Refinery, as well as in the Bank of Ghana (the central bank). In the state-owned enterprises, quasi-fiscal activities are reflected in mispricing, commercial and excessive technical losses (for example, from unbilled consumption and theft), and the accumulation of new payment arrears. In the Bank of Ghana, they are evident in the relatively high cost of conducting open market operations (although declining interest rates have recently reduced the cost) and sterilizing strong capital inflows, as well as in the absence of remuneration on commercial banks' deposits held in the central bank to satisfy the primary reserve requirement.

Ghana's combined quasi-fiscal activities reached the equivalent of about 6¾ percent of GDP in 2002 before declining to about 2¾ percent of GDP during 2004 (see table). In 2002, two activities accounted for nearly two-thirds of this amount: the government's below-cost pricing of petroleum products, which made it impossible for the Tema Oil Refinery to recover its refining costs; and the Volta River Authority's below-cost pricing of electricity, reflected in a substantial

Still too great a presence

Quasi-fiscal activities have declined but still pose a problem.

	2000	2001	2002	2003	2004
	(percent of GDP)				
Nonfinancial public enterprises	0.5	0.8	7.2	4.2	2.1
Tema Oil Refinery	...	0.0	1.8	0.3	0.0
Volta River Authority	3.3	2.0	0.4
Electricity Company of Ghana	1.2	1.1	1.1
Ghana Water Company Limited	0.5	0.7	0.9	0.8	0.7
Bank of Ghana	-0.7	-0.7	-0.5	0.0	0.6
Total	-0.2	0.1	6.7	4.2	2.7

Data: Authors' calculations.

discount to its largest customer. Although quasi-fiscal activities have been reduced, they are still significant enough to dampen the financial prospects of the public sector.

If the financial performance of the major state-owned enterprises, which is driven largely by quasi-fiscal activities, is combined with that of the central government, the picture of Ghana's fiscal situation differs from that based on the central government's finances alone. The overall deficit of the public sector averaged 9 percent of GDP during 2000–04, compared with 6½ percent of GDP for the central government. To finance the large deficits, Ghana borrowed, accumulating domestic debt for the broader public sector amounting to 37 percent of GDP by end-2003, compared with just over 18 percent for the central government alone.

Preliminary data suggest that, despite the additional debt, the government reached its medium-term objective of halving the ratio of domestic debt to GDP by end-2005 from its end-2002 level—mainly by reducing the central government debt. More recently, the strength of fiscal consolidation combined with satisfactory performance of some state-owned enterprises has led to a significant decline of the public sector deficit (see chart).

Implications for economic performance

In general, governments use quasi-fiscal activities to achieve a variety of social, political, and economic objectives. Although some of the objectives are worthwhile, quasi-fiscal activities have broad economic and policy implications:

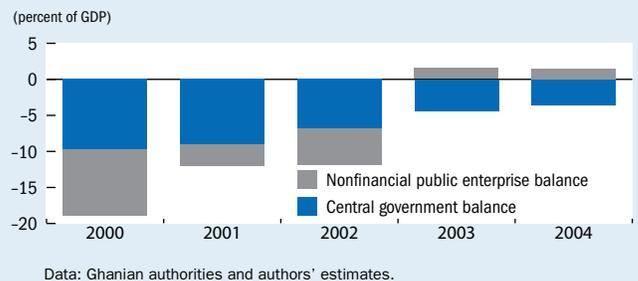
- They may understate the size of government.
- They can create contingent government liabilities.
- They often escape legislative and public scrutiny.
- They can contribute to monetary expansion and may have the same adverse effects as the financing of government expenditures, such as crowding out.
- Through moral hazard, they may have adverse effects on the financial system, under the presumption of a government bailout.
- They distort resource allocation and generate unwanted and nontransparent redistribution, with implications for equity and economic growth.

Quasi-fiscal activities in Ghana have a number of undesirable effects, which the government needs to address to improve fiscal sustainability and economic performance.

The poor performance of public enterprises imposes both a financial and an economic burden on the country, raising the public sector borrowing requirement and putting upward pressure on interest rates. In turn, higher interest rates impede private sector investment, development, and productivity growth. Without efficient public enterprises, Ghana is unlikely to undertake the investments required to upgrade its

Trimming the debt

Fiscal discipline, including a decline in quasi-fiscal activities, is helping to reduce the public sector deficit.



public infrastructure—particularly in the energy sector and utilities—which will also have adverse consequences for private investment and economic growth.

The Bank of Ghana's failure to remunerate commercial banks' primary reserve requirements is equivalent to a quasi-fiscal tax, which represents forgone revenue to the budget. However, the relatively high cost of sterilizing capital inflows more than offsets the lack of remuneration, giving rise to quasi-fiscal losses for the Bank of Ghana rather than any transfer of profits and dividends to the budget.

Quasi-fiscal activities have seriously distorted energy and water consumption, as well as the investment decisions of both the affected public enterprises and the private sector. In addition, they have a negative effect on equity and fairness, such as the preferential prices previously offered by the Volta River Authority to its largest customer.

The budget must eventually absorb these quasi-fiscal losses, which suggests the government will have less scope to increase spending on growth-enhancing and poverty-reducing social programs to achieve the Millennium Development Goals. Although improvement will take time, the government recognizes the urgent need to improve the financial and operating performance of the remaining public enterprises. As a first step, it has liberalized the prices of petroleum products, effectively eliminating quasi-fiscal activities from the Tema Oil Refinery, and it is implementing measures to enhance revenue collection and ensure that the prices charged by public utility companies are set to recover costs fully. ■

Mali Chivakul and Robert C. York

IMF Monetary and Financial Systems and African departments

Copies of IMF Working Paper No. 06/24, "Implications of Quasi-Fiscal Activities in Ghana," by Mali Chivakul and Robert C. York, are available for \$15.00 each from IMF Publication Services. Please see page 96 for ordering details. The full text is also available on the IMF's website (www.imf.org).

Africa in the Doha Round: Dealing with preference erosion and beyond

Many African countries face a dilemma in the World Trade Organization's (WTO) current Doha Round of trade negotiations. On the one hand, they want industrial countries to open their markets further, and, on the other, they are apprehensive about losing preferential access to these markets as a result of multilateral liberalization. How can African countries deal with preference erosion and pursue their interests under the Doha Round? A new IMF Policy Discussion Paper argues that they should seek greater market access—not only in industrial countries but also in developing countries—and strengthen their commitment to liberalization.

Where should Africa seek greater market access and for which products? Part of the answer lies in the continent's pattern of trade, which has shifted over the past 25 years. While industrial countries have remained the continent's dominant export market and intra-African exports have remained low, developing countries, especially those in Asia, have become the continent's fastest-growing export market. Equally significant is the increasing share of Africa's imports that come from developing countries (see chart). Moreover, these countries have become an important source of foreign direct investment and technology transfer, which are closely linked to Africa's export industries, such as commodities and clothing. Assuming that these trends continue, Africa has an ever-increasing interest in trade reform in these countries.

Africa's export composition, dominated by primary commodities, also has a bearing on the continent's negotiation strategy in the Doha Round. Agricultural products account for over one-fourth of its total exports. This implies, first, that because most-favored-nation tariffs on most industrial goods in developed countries are already low, most African countries will probably benefit more from agricultural liberalization, at least in the long run. Members of the Organization for Economic Cooperation and Development (OECD), except for the European Union (EU) members, still maintain high protection against African agricultural exports. Therefore, the potential benefits of market access in the full OECD can be large. However, benefits are likely to accrue mainly to current net exporters of agricultural products. Indeed, some net agricultural importers may lose, particularly in the short to medium term, as a result of rising world prices following trade liberalization.

In the industrial goods sector, Africa generally faces low tariffs in Canada, the EU, Japan, and the United States but much higher tariffs in developing countries and many other



Senhou/AFIP/Getty Images

Women prepare cakes of fresh-caught tuna in Senegal for export as part of an effort to spur development in Africa.

OECD member countries. Thus, the potential benefits of improved market access for manufactures in developing countries are significant.

Perhaps the largest potential benefits for African countries will come from liberalizing their own trade. Despite steady cuts over the past decades, Africa's tariffs are higher than those in other developing regions. In addition, only a fraction of its tariffs are bound (committed in the WTO), and, where they are, they are often considerably higher than their applied rates.

Quantifying the benefits

To what extent can African countries derive benefits from the Doha Round by liberalizing their own trade and from demanding greater market opening by their trading partners? Drawing on a recent World Bank study by Kym Anderson, Will Martin, and Dominique van der Mensbrugge, the paper examines the Doha Round's possible impact on African countries. The study simulates four trade liberalization scenarios that progressively broaden country and sector coverage and deepen tariff cuts to show how liberalization would affect African countries in each country group (industrial and developing) and sector (agriculture and industry).

Scenario 1: Only agricultural trade is liberalized. The average agricultural tariff is cut by 44 percent for developed countries as a group and by 21 percent for developing countries. Agricultural export subsidies are eliminated completely.

Scenario 2: In addition to the liberalization under Scenario 1, nonagricultural tariffs are cut by 50 percent in high-income countries, 33 percent in developing countries, and not at all in the least developed countries.

Scenario 3: Developing countries (including the least developed ones) fully participate in the Doha Round by reducing their bound (not necessarily applied) tariffs by the same percentage as the high-income countries in Scenario 2.

Scenario 4: Full liberalization.

What happens? Under Scenario 1, the bulk of the increased world income accrues to high-income reforming countries, which recoup the efficiency losses from their own policy distortions. The gains (largely coming from terms of trade improvement) for sub-Saharan African (SSA) countries are only \$0.4 billion, less than 1/10 of 1 percent of their initial income. This result highlights the limitations of SSA countries' reliance on improved market access in industrial countries during the Doha Round—even in the highly distorted agricultural sector.

In Scenario 2, the gains nearly double for SSA as a group, but some countries suffer a small loss. The latter outcome points to the possibility that some African countries stand to lose if the resulting increases in preference erosion in industrial countries are not offset by improved market access elsewhere. At the same time, the overall outcome highlights the importance of developing country markets, in which even moderate tariff reductions would significantly increase market access for the continent as a whole.

In Scenario 3, the gains to SSA countries more than quadruple—to nearly 0.3 percent of their income—even though their ambitious cuts of bound tariffs do not reduce applied tariffs by much.

In Scenario 4, SSA's gains would more than quadruple again, to more than 1 percent of its initial income.

Clearly, Africa's own liberalization, along with that of other developing countries, is critical if the poorer SSA countries are to achieve a positive Doha Round outcome. The nega-

Africa's own liberalization, along with that of other developing countries, is critical if the poorer sub-Saharan African countries are to achieve a positive Doha Round outcome.

tive effects of preference erosion can easily be overcome if SSA countries reduce their applied tariffs—even if only moderately—by substantially lowering their bound rates. Liberalization by industrial countries is also important, but its impact is perhaps best seen in terms of their influence over the overall liberalization commitments in the Doha Round, as well as the direct market access they can offer to African countries.

The importance of tariff cuts by developing countries outside SSA is also evident from their impact on Africa's exports. In Scenario 2, without the combined expansion of agricultural and nonagricultural exports to developing countries, including SSA countries themselves, the increase in agricultural exports to high-income country markets would not be able to completely offset the decline in industrial goods exports—a result that reflects the effect of preference erosion. Equally important, developing countries would provide nearly half of the import increase that SSA countries need if they are to achieve the overall positive income result under this scenario.

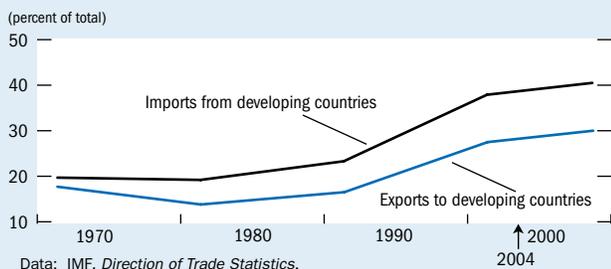
What it all means

Preference erosion would be an inevitable result of Doha Round liberalization, but a defensive strategy to minimize erosion will provide no lasting solution. A comprehensive reduction in trade barriers across all WTO members would best serve Africa's interests. To this end, African countries, including the least developed ones, which are not required to cut their own tariffs in the Doha Round, need to focus on reciprocal liberalization.

Africa's firm and ambitious commitment to bind and reduce its own tariffs would help reduce the antiexport bias of its trade policies (since import tariffs are equivalent to a tax on exports) and create the more favorable investment climate that many African countries desperately need. It would also strengthen African countries' position in the trade negotiations and enable them to demand the special and differential treatment they need to help smooth structural adjustment. Moreover, ambitious reforms would provide a more compelling basis for asking for aid for trade, which would help improve Africa's ability to expand its export opportunities by improving its domestic supply response and increase its export competitiveness. ■

Trading places

Africa's trade with developing countries has grown markedly over the past two and a half decades.



Copies of IMF Policy Discussion Paper No. 05/8, "Africa in the Doha Round: Dealing with Preference Erosion and Beyond," by Yongzheng Yang, are available for \$15.00 each from IMF Publication Services. Please see page 96 for ordering details. The full text is also available on the IMF's website (www.imf.org).

Euro area needs to ease product market regulations to stimulate growth

Real wage growth in the euro area has moderated since the 1970s, particularly over the past decade. Such wage moderation helps to contain production costs and support firms' profitability and can thus lead to reduced unemployment and increased output. But unemployment in the euro area has declined only slightly since the mid-1990s, and per capita GDP growth has fallen—a puzzling development that raises questions about the benefits of wage moderation. In a recent IMF Working Paper, Marcello Estevão examines the relationship among wages, unemployment, and output growth. He finds that wage moderation does spur output and lower unemployment but that the magnitude of these effects depends on the degree to which countries' product markets are regulated.

The annual growth of real hourly employee compensation in the euro area's business sector has declined from about 6 percent at the beginning of the 1970s to 1 percent recently. Unemployment rates began to recede in the mid-1990s, bottomed out at about 8 percent in 2001, but have since climbed to about 9 percent. And annual growth in per capita business GDP has declined from an average of 3 percent in the 1970s to about 1.9 percent in the past 10 years. Why has the apparent moderation of wages in the euro area not made firms more profitable and led to faster production growth?

The wage-growth puzzle

Simple correlations from cross-country data for the euro area from 1983 to 2003 suggest that real wage changes have a weak relationship with unemployment and are positively related to output. They suggest that, if real wages decline, both the unemployment rate and GDP per capita growth also decline. However, Estevão says, such raw correlations between real wage changes and economic performance may capture forces other than those associated with structural changes in wage-setting behavior. For example, changes in wages can affect economic activity by influencing workers' income and, thus, their consumption, which would cause wages and output to be positively correlated in the short run. In addition, the costs of being unemployed diminish during good times because those who lose jobs in one business have a high probability of being hired by another business. In this situation, workers would demand higher wages, which could again lead to a positive correlation between output growth and real wage growth.

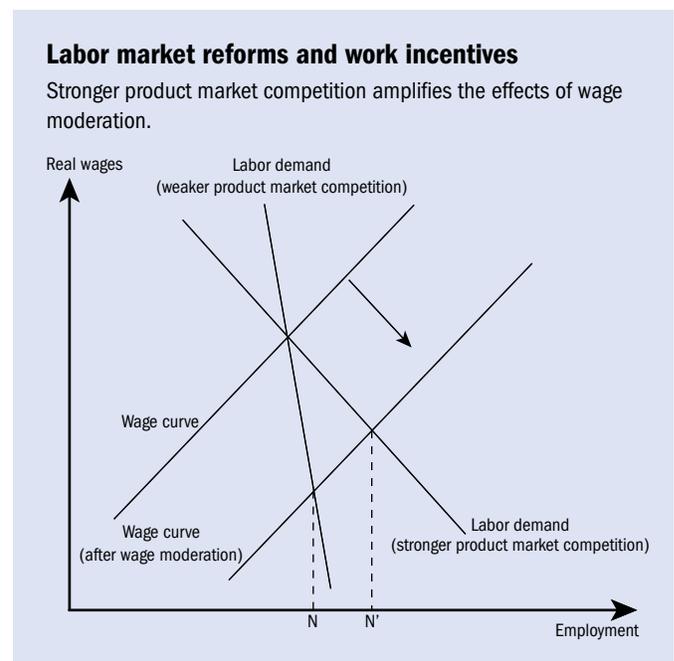
To unravel the relationship between shifts in wage-setting behavior and unemployment, Estevão looked at 20 industrial countries using a standard bargaining model—according to

which workers and firms negotiate wages, and the goal of firms is to maximize profits—to isolate structural changes in the relationship between wages and unemployment rates—a “wage curve”—and the effects of the changes on production costs. In this theoretical framework, the wage curve may shift for several reasons, including when labor market reforms increase incentives to work (see diagram).

According to the model, downward shifts in the wage curve, representing increases in wage moderation, are associated with higher employment rates and higher per capita GDP growth. Wage moderation generates higher profits, encouraging new firms to enter the market and existing firms to invest more, thereby resulting in higher output. What might cause increased wage moderation? Possible factors include reductions in unemployment benefits; declines in workers' bargaining power, which might occur because of the expansion of the labor pool through globalization; changes in unions' preferences away from wages toward employment; and lower labor-income taxes, which would allow firms to offer lower wages while workers' net take-home pay would rise.

How regulations affect product markets

The model also suggests that regulations that curb competition will tend to dampen the positive effects of wage moderation on economic performance. Regulations can operate through a short-term competition effect on firms' pricing



power, for example, from direct government intervention in pricing; and through a long-run market contestability effect, such as barriers to entry, that curbs potential new entrants and affects competition among existing firms. Moreover, a large concentration of state-owned companies and other state interventions could distort market signals and slow output responses to cost shocks. Thus, an improvement in wage-setting conditions in less regulated product markets may generate fiercer competition for market share. In the process, output and employment increase more in these markets. In more regulated product markets, though, softer competition pressures may lead existing firms to expropriate a larger share of the cost reduction in the form of higher profits.

Estevão's econometric evidence supports the finding that restrictions on product market competition dampen the effects of wage moderation, which is consistent with a link between product market regulation and firms' rent-seeking behavior. Such restrictions vary over time and from country to country, causing large disparities in the effects of wage moderation. Over the past 20 years, wage moderation has indeed varied considerably among the 20 countries and, in particular, within the euro area. It has also had different effects on countries' economic performance, depending on the extent of product market regulation.

Overall, Estevão found that wage-setting conditions had improved at least since the 1990s, except in Greece, Japan, and Switzerland. Ireland stands out because its wage-setting conditions have improved dramatically and continuously since the 1970s. In the euro area, wage setting has improved significantly in the Netherlands since the early 1980s and in Finland since the early 1990s. Wage moderation has occurred

in France and Italy since the 1980s and in Belgium, Germany, and Spain since the mid-1990s. Outside the euro area, wage setting deteriorated through the early 1980s in Australia, Canada, the United Kingdom, and the United States but has since improved steadily.

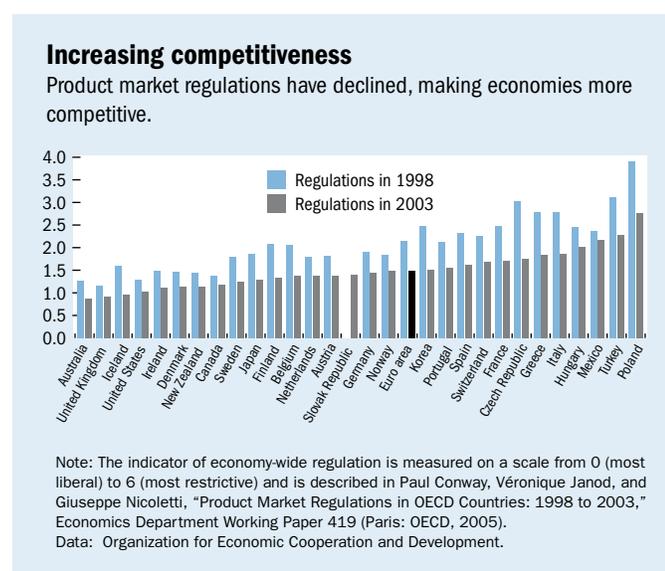
As for regulatory developments in product markets, they became more flexible between 1975 and 1998, increasing the pass-through from wage moderation to growth and employment. Different data for economy-wide product market regulation for only two years (1998 and 2003) suggest that impediments to product-market competition have declined further (see chart). And, in particular, the extent of government involvement in product markets and barriers to international flows of capital and trade have fallen considerably since 1998.

Euro area should liberalize more

Still, important cross-country differences persist, and further product market liberalization within the euro area would increase the benefits of labor market reforms. According to Estevão's data, 8 euro area countries were among the 10 most heavily regulated industrial economies in 1998. Thus, wage moderation in the region was, on average, less effective in raising GDP growth and lowering unemployment.

Estevão presents empirical evidence that product market reforms increase the economic benefits of labor market reforms, thus making them more politically acceptable. These findings are consistent with previous work on the complementarity between reforms of the two kinds of markets. Some studies suggest that product market reforms should come first because, by lowering barriers to entry and fostering competition, they tend to increase real wages and reduce unemployment. Higher real wages would buy goodwill from unions and ease implementation of labor market reforms, which sometimes have a negative wage effect in the short run.

Overall, heavily regulated product markets are undermining the effectiveness of labor market reform in the euro area. Although product markets in virtually all industrial countries have become more market friendly over the past 30 years, policy approaches and results continue to differ, including within the euro area. Without additional liberalization in this area, wide segments of society may continue to resist calls for more labor market reforms to lower unemployment and increase production. ■



Copies of IMF Working Paper No. 05/191, "Product Market Regulation and the Benefits of Wage Moderation," by Marcello M. Estevão, are available for \$15.00 each from IMF Publication Services. Please see page 96 for ordering details. The full text is also available on the IMF's website (www.imf.org).

FDI flows to Asia: Did the dragon crowd out the tigers?

In recent years, China has topped the list of destinations for foreign direct investment (FDI) among developing and emerging market countries. But has its stellar performance come at the price of reduced FDI elsewhere in Asia? Generally, no, argues a new IMF Working Paper, although Singapore and Myanmar may be exceptions.

Many developing countries have been eager to attract FDI flows, which are not as volatile as other types of capital flows, tend to boost technology transfers and raise growth rates, and can spur domestic investment. China's success in attracting FDI has been impressive. Only 25 years ago, China's share of FDI in developing Asia was about 10 percent. By 2002, the country's share was 70 percent (see chart).

With success, however, have come fears that China has diverted flows from other countries in the region. For a clearer sense of what has, in fact, happened, our study, using a new methodology, analyzed data for 1984–2002 for 14 Asian economies (Bangladesh, China, India, Indonesia, Korea, Malaysia, Myanmar, Papua New Guinea, Philippines, Singapore, Sri Lanka, Taiwan Province of China, Thailand, and Vietnam).

The study found that, on average, China does appear to have diverted FDI flows during this period. Between the early 1990s, when China began opening its doors to FDI, and 2002, flows to other countries declined by an average of 1.3 to 2.1 percent of GDP a year, depending on the estimation method used. A closer look suggests, however, that this crowding out was concentrated in two countries—Singapore and Myanmar.

Favorite among Asian emerging markets

By the early 2000s, more than 70 percent of foreign direct investment in emerging markets in Asia went to China.



What explains the change in flows?

Singapore and Myanmar experienced large declines in FDI inflows—between 1.9 percent and 2.8 percent, and 3.9 percent and 4.5 percent of GDP a year, respectively. For Singapore, the most probable explanation for the decline seems to lie in the role played by overseas Chinese. They account for a significant share of foreign investment in China and invest because they have family connections or, at least, linguistic and cultural ties. Some overseas Chinese are similarly connected to Singapore. If these investors focus their investment on regions to which they are connected, a decision to invest in China might indeed come at the expense of Singapore.

Myanmar's situation is trickier. Political developments there have led many traditionally large suppliers of FDI (including the United States and the European Union) to severely restrict FDI in Myanmar. The imposition of new restrictions plays a role in the dynamics of foreign investment in the country but is obviously unrelated to China. A more likely possibility is that Singapore, the second-largest foreign investor in Myanmar, may have diverted some of its FDI to China at Myanmar's expense (China and Hong Kong SAR are the two main destinations for Singaporean investment).

It is also sometimes argued that low-income economies, which compete with China for low-wage investment, suffer more from China's competition, while countries that invest more in human capital and research and development are less affected. The study tests these assumptions, with the results suggesting that low-income economies did not suffer more from diversion of FDI than higher-income ones. Low levels of secondary or tertiary education or fewer scientific publications per person are not associated with increased crowding out by China either.

China's emergence as a major destination for FDI flows did not, during the period studied, seem to have a negative impact on most of its neighbors. The sheer size of China and the likelihood that India may soon follow in its footsteps make it important, however, to continue analyzing the regional and global impact of these two demographic giants. ■

Benoît Mercereau
IMF Asia and Pacific Department

Copies of IMF Working Paper No. 05/189, "FDI Flows to Asia: Did the Dragon Crowd Out the Tigers?" by Benoît Mercereau, are available for \$15.00 each from IMF Publication Services. Please see page 96 for ordering details. The full text is also available on the IMF's website (www.imf.org).

Stand-By, EFF, and PRGF arrangements (as of February 28, 2006)

Member	Date of arrangement	Expiration date	Amount approved	Undrawn balance
(million SDRs)				
Stand-By				
Bolivia	April 2, 2003	March 31, 2006	145.78	34.28
Bulgaria	August 6, 2004	September 5, 2006	100.00	100.00
Colombia	May 2, 2005	November 2, 2006	405.00	405.00
Croatia	August 4, 2004	April 3, 2006	97.00	97.00
Dominican Republic	January 31, 2005	May 31, 2007	437.80	288.94
Iraq	December 23, 2005	March 22, 2007	475.36	475.36
Macedonia, FYR	August 31, 2005	August 30, 2008	51.68	41.18
Peru	June 9, 2004	August 16, 2006	287.28	287.28
Romania	July 7, 2004	July 6, 2006	250.00	250.00
Turkey	May 11, 2005	May 10, 2008	6,662.04	4,996.53
Uruguay	June 8, 2005	June 7, 2008	766.25	674.30
Total			9,678.18	7,649.86
EFF				
Albania	February 1, 2006	January 31, 2009	8.52	7.31
Sri Lanka	April 18, 2003	April 17, 2006	144.40	123.73
Total			152.92	131.04
PRGF				
Albania	February 1, 2006	January 31, 2009	8.52	7.31
Armenia	May 25, 2005	May 24, 2008	23.00	16.44
Bangladesh	June 20, 2003	December 31, 2006	400.33	117.27
Benin	August 5, 2005	August 4, 2008	6.19	5.31
Burkina Faso	June 11, 2003	August 15, 2006	24.08	6.88
Burundi	January 23, 2004	January 22, 2007	69.30	28.60
Cameroon	October 24, 2005	October 23, 2008	18.57	15.92
Chad	February 16, 2005	February 15, 2008	25.20	21.00
Congo, Democratic Republic of	June 12, 2002	March 31, 2006	580.00	26.53
Congo, Republic of	December 6, 2004	December 5, 2007	54.99	39.27
Dominica	December 29, 2003	December 28, 2006	7.69	2.32
Georgia	June 4, 2004	June 3, 2007	98.00	56.00
Ghana	May 9, 2003	October 31, 2006	184.50	79.10
Guyana	September 20, 2002	September 12, 2006	54.55	9.25
Honduras	February 27, 2004	February 26, 2007	71.20	30.52
Kenya	November 21, 2003	November 20, 2006	225.00	150.00
Kyrgyz Republic	March 15, 2005	March 14, 2008	8.88	6.35
Mali	June 23, 2004	June 22, 2007	9.33	4.01
Malawi	August 5, 2005	August 4, 2008	38.17	32.75
Mozambique	July 6, 2004	July 5, 2007	11.36	4.88
Nepal	November 19, 2003	November 18, 2006	49.91	35.65
Nicaragua	December 13, 2002	December 12, 2006	97.50	27.85
Niger	January 31, 2005	January 30, 2008	26.32	14.57
Rwanda	August 12, 2002	June 11, 2006	4.00	0.57
São Tomé and Príncipe	August 1, 2005	July 31, 2008	2.96	2.54
Senegal	April 28, 2003	April 27, 2006	24.27	-
Sri Lanka	April 18, 2003	April 17, 2006	269.00	230.61
Tanzania	August 16, 2003	August 15, 2006	19.60	5.60
Zambia	June 16, 2004	June 15, 2007	220.10	33.01
Total			2,632.52	1,141.14

EFF = Extended Fund Facility.

PRGF = Poverty Reduction and Growth Facility.

Figures may not add to totals owing to rounding.

Data: IMF Finance Department

Prescriptions for financial stability

Everyone recognizes a financial crisis. But financial stability, according to the IMF's Garry Schinasi, is more difficult—but not impossible—to define, measure, and monitor. In a new IMF publication, *Safeguarding Financial Stability: Theory and Practice*, he addresses these issues and develops a framework for assessing national and international financial stability.

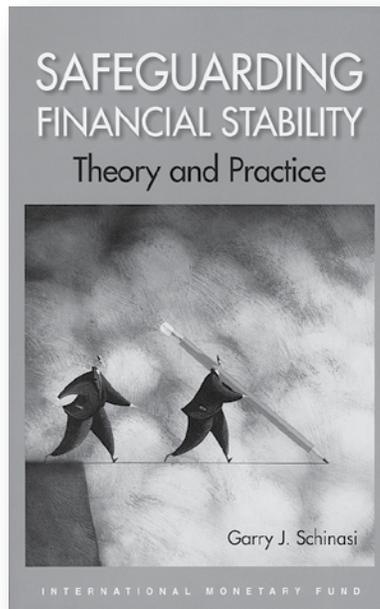
A 10-year veteran of international capital market surveillance, Schinasi saw a need for such a framework. His book offers a comprehensive approach—analysis of macroeconomic and financial conditions and of institutions, markets, and infrastructures—for evaluating the sources of risk and vulnerability in financial systems. The framework is not a blueprint but a more generic tool that can be adapted to countries' needs. It relies on coordinating sources of information and formalizing the information into an assessment. "It's a conceptual and analytical approach to evaluating what problems might arise, thinking about the policies required to deal with the problems, and putting changes in place to prevent them from recurring," he says.

Schinasi sees the assessment process as continuous and organic, and he uses a medical analogy to explain it. Financial stability is akin to human health, he says. A person who is healthy and wants to maintain good health needs to be in preventive mode. Similarly, a country that is showing no signs of becoming unstable in the near future should also be in preventive mode, maintaining and updating its policies to prevent future imbalances.

A patient with symptoms may not be ill but may nonetheless require remedial action. If a market is showing symptoms, the authorities responsible for market surveillance would assess the problem. What is causing spikes in asset prices? Why is everyone selling? Is it a market dis-

location requiring remedial action, or will it work itself out?

Then there is the resolution mode. The patient gets sick and requires surgery. The treatment may cause the patient to get worse before he gets better. Like a doctor, a country's financial authorities will intensify their policies as the financial system moves toward, or crosses, the boundary of stability.



The book also takes up the benefits and challenges of modern finance; it draws on a rich vein of real-world experiences—the growing reliance on over-the-counter derivatives, the growth of credit derivatives, and the capital market activities of insurers and reinsurers. Schinasi says, "We've learned how the advanced markets have evolved, how they've innovated, and what risks come with innovation." Much of the rest of the world will go through its own cycles of innovation and should benefit from the lessons that have emerged so far.

The book has three audiences: policymakers at central banks, supervisory authorities, and finance ministries; IMF staff engaged in financial surveillance; and graduate students studying economics, finance, and public policy. Unable to find a book to prepare people to work on financial stability issues, Schinasi drew on his experience to write one. Still, he doesn't consider his framework the definitive approach. Rather, he sees it as the start of a debate. People should read the book and think about the issues. "If a better way to safeguard financial stability is developed as a result," he says, "that would be great." ■

Elisa Diehl
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Copies of *Safeguarding Financial Stability: Theory and Practice*, by Garry J. Schinasi, are available from IMF Publication Services for \$28.00 each. See this page for ordering information.



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