DEPARTMENTS

Illustration: Cover and p. 8, Terry Widener; pp. 14, 17, 24, and 29, Richard Downs.

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FROM THE EDITOR

Risky behavior

WHAT started as a subprime mortgage crisis in the United States in summer 2007 is still being felt, nearly a year later, in a surprising variety of places—such as markets in which banks make loans to one another, short-term commercial paper, municipal bonds, and even student loans, and not only in the United States. The financial turmoil—now global—continues to raise worries about global financial stability, prompting F&D to ask: How did the crisis spread, and what can be done to minimize the likelihood of this type of financial crisis and ensuing contagion occurring again?

In our June issue, we tackle this question from a number of angles. Our lead story, "A Crisis of Confidence ... and a Lot More," argues that the source of the problem and, hence, the solution lie in "incentives, incentives, incentives." But, that said, the remedies won't be easy to implement, given that faulty incentives are already entrenched in the marketplace and in regulatory and supervisory systems—incentives that encouraged traders, investors, and loan originators to take way too many risks, which were often camouflaged by opaque, complex securities and facilitated by too much leverage and lax credit standards.

As policymakers debate ways to reshape incentives, the authors of "Outbreak: U.S. Subprime Contagion" suggest that they keep the following objectives in mind: moderate leverage, improve liquidity management, foster market liquidity, promote due diligence, and increase transparency. And they note that a key lesson is that risk management at individual banks shouldn't be focused so narrowly on protecting the institution that systemic risks are largely ignored. Two other articles explore the debate surrounding steps being taken to shore up banking systems. At the center of the debate is the ongoing implementation of what is known as Basel II—an international standard for the amount of capital that banks need to put aside to deal with current and potential financial and operational risks.

From the Monetary Authority of Singapore, we get an Asian take on the similarities and differences between the 1997–98 Asian financial crisis and the U.S. subprime crisis—plus thoughts on what Asia and emerging markets generally can do to maintain their resilience to the current financial turmoil.

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Finally, with the June issue, I am stepping down as Editor-in-Chief of F&D after six-and-a-half years. I have immensely enjoyed the challenges of guiding this publication—especially putting together four thought-provoking issues a year that give our highly diverse readership a taste of the critical financial, economic, and development issues facing the international community. I hope that you've enjoyed the packages that my wonderful team has assembled, and I'd like to thank all of you for your comments, suggestions, and support over the years.

Laura Wallace
Editor-in-Chief