In the aftermath of the terrorist attacks of September 11, a coordinated international response is needed to deal with weaknesses in the world economy and the new risks in the outlook,” IMF Managing Director Horst Köhler said in a statement issued on October 5. He added that “the IMF, its 183 member countries, and the international community more generally will need to respond with sound policies to reduce the likelihood of a sustained slowdown and make sure we are ready to deal with a deeper and longer downturn if it does emerge—thereby limiting the disruption and attendant human costs.” Excerpts from Köhler’s statement follow.

In the immediate future, economic policies will need to be framed in an environment of unusually large uncertainty. There are good reasons to expect that the current deterioration of economic conditions may be relatively short-lived, with an upturn commencing in the first half of 2002. These include the improved fundamentals that were already present in the global economy, the policy response that has taken place, and the scope for further policy adjustments, if necessary. But there is also a nonnegligible probability of a worse outcome, involving lower growth and increasing financing difficulties for many countries. In this context, we see the following framework for a coordinated response.

Global outlook and risks

Notwithstanding the uncertainty, a number of developments indicate that a more pronounced than expected economic slowdown is under way across much of the IMF’s membership. Even before the attacks on September 11, the global situation was weak, with a synchronized downturn across all major regions . . . as noted in the IMF’s latest World Economic Outlook [see IMF Survey, October 8, page 309].

In the aftermath of the attacks, there will be an impact on activity, particularly in the United States, but also elsewhere. The situation of emerging markets and developing countries has become more difficult, with reduced access to global financial markets, and deeper demand and commodity price declines. In addition, security concerns after the attack are translating into higher costs for airline transport (related to security measures), lower tourism owing to safety concerns, and higher prices and higher transportation costs for merchandise. Finally, the impact on oil prices could be substantial in either direction.

There are intensified downside risks to world economic and financial...
Role of the IMF
The IMF has appropriate tools and flexibility to respond to a weakening world economy. In the context of its overall approach of surveillance and lending, the IMF can take a number of concrete steps. We are closely monitoring the situation, with early and proactive dialogue with member countries. I encourage all members to review their policy frameworks in light of recent developments and to approach the IMF early to discuss the implications of these developments for their economic policies. The appropriate response by the IMF will depend on the member countries involved and the nature of the problems they confront. While the IMF’s existing financial instruments and policies appear adequate, the IMF will be ready to adjust its policies if necessary.

• Advanced economies have a key responsibility to ensure that macroeconomic and financial policies support an early return to sustainable growth and financial strength. There has been a significant easing of monetary policy in the United States and most other advanced countries, and its impact should be felt increasingly in the coming months. In Japan, there is still scope for more decisive monetary action. In addition, the restoration of confidence in Japan will clearly require resolute steps on banking sector and corporate restructuring. In the euro area, automatic stabilizers should be allowed to work fully. Monetary policy

should be vigilant and, if necessary, use the room for additional easing. In addition, consumer and investor confidence would be enhanced by an acceleration of structural measures to improve growth potential.

• Emerging market economies are exposed to shocks to both the current and capital accounts, and the availability of private financial flows is a key vulnerability. Sound economic policies, including early adjustment when needed, are imperative. For its part, the IMF can approach eligible countries to encourage consideration of Contingent Credit Lines to help them face potential contagion effects in capital market conditions; consider new programs supported by the Supplemental Reserve Facility and/or Stand-By Arrangements in those economies where it is deemed appropriate; and, for countries with existing programs, consider augmenting or rephasing access when the policy framework is strong and appropriate for the emerging circumstances.

• Developing economies are exposed to current account shocks derived from weaker commodity prices and lower demand for their exports of goods and services. The IMF stands ready to help these countries design appropriate policy responses.

• Low-income countries are exposed to shocks similar to those of other developing countries. While the policy response in terms of adjustment may be the same, the terms of additional financing should not. The IMF would stand ready to make available additional concessional resources, using the Poverty Reduction and Growth Facility (PRGF) where a three-year program is in place or can be agreed to early on. For members not ready to undertake a three-year structural reform program, Stand-By Arrangements may be considered. We could also encourage countries to seek additional concessional resources where necessary from other official sources and work with creditors to encourage a positive and well-coordinated response, including assistance under the Heavily Indebted Poor Countries (HIPC) Initiative.

Overall, the IMF’s existing financial instruments and policies appear adequate to address the needs of its membership, and the IMF will be ready to adjust its policies quickly if necessary. While the prospective demand for IMF resources is sensitive to the size of the downturn and assumptions about market access for emerging market countries, the IMF has the capacity to respond to the evolving situation in its member countries in the period ahead.

Recent developments have, however, made more urgent the need to complete the financing package for the interim PRGF to enable the IMF to continue assisting low-income countries on appropriate terms. If demand exceeds earlier tightly constrained projections, it may be necessary to mobilize additional PRGF sub-

IMFC, Development Committee meetings to be held November 17-18 in Ottawa
On October 17, IMF Managing Director Horst Köhler and World Bank President James D. Wolfensohn—after consultation with the institutions’ Boards of Executive Directors, and with Gordon Brown, the chair of the International Monetary and Financial Committee (IMFC), and Yashwant Sinha, the chair of the Development Committee—announced that they were “pleased to accept the invitation made by the Canadian Finance Minister, Paul Martin, to host meetings of the IMFC and DC in Ottawa on November 17-18.”

They also noted that “these meetings will bring together ministers and central bank governors from around the world to discuss issues of importance to the membership of the IMF and the World Bank, especially including the global economic outlook in the wake of the tragic events of September 11; their impact, in particular, on the poorest; the ongoing work to improve the stability of the international financial system; and preparations for the forthcoming United Nations Conference on Financing for Development.”

The full text of IMF News Brief 01/103 is available on the IMF’s website (www.imf.org).
sidy and loan resources or to accelerate the interim PRGF at the expense of the level of self-sustained PRGF operations. We should not let that eventuality hinder our support for low-income members in the immediate circumstances.

**Worldwide response**
The IMF’s response should be part of a concerted response by the international community. The engagement of a whole spectrum of institutions would be needed, in particular:

- Multilateral development banks’ participation will be essential for appropriate sectoral advice and because additional project and program financing and budgetary support may be needed in some countries. For this reason, I have joined with the presidents of the World Bank and the four regional development banks to set out our coordinated response to these events.
- Export credit agencies will need to play their role in helping to ensure the continued availability of trade finance.
- The Paris Club may need to be involved, as the solution to the external financing needs of some members may entail rescheduling obligations to official creditors.
- Reengagement of the private international capital markets will be a key to a more rapid recovery. The Capital Markets Consultative Group, which is scheduled to meet again in mid-October, is an important vehicle for reaching out to the private sector.

- To bolster confidence, the launching of a new trade round is of critical importance. It is equally important not to lose momentum on various industrial country initiatives to increase the access of the poorest countries to their markets.
- Efforts to vigorously implement global anti-money laundering initiatives should be fully endorsed. In concert with the broader efforts of other institutions, the IMF is further strengthening its role in the anti-money laundering effort. In light of the terrorist attacks, the organization’s management has just established an internal task force of IMF staff, chaired by a Deputy Managing Director, to examine urgently the IMF’s contributions to the worldwide effort against money laundering.

To lead this coordinated approach to the deteriorating world situation, the international community should meet. I therefore support holding an early meeting of the International Monetary and Financial Committee [see page 326].

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**Group of Seven**

**Economic leaders express confidence about future, unveil plan to combat terrorist financing**

Finance ministers and central bank governors of the Group of Seven industrial countries met on October 6 in Washington, DC, to discuss international efforts to combat the financing of terrorism and to address the impact the September 11 attacks may have on the global economy. In addition to a statement issued at the end of the one-day meeting, the Group of Seven ministers and governors also released their Action Plan to Combat the Financing of Terrorism (see page 328).

In their statement, ministers and governors said, “we stand united in our commitment to vigorously track down and intercept the assets of terrorists and to pursue the individuals and countries suspected of financing terrorists. We will implement United Nations (UN) sanctions to block terrorist assets.” [See related story, page 329.] Group of Seven officials said they were encouraged by the number of countries throughout the world that have already joined in international action to wage a successful fight against the financing of terrorism and welcomed the decision by the Financial Action Task Force to hold an extraordinary plenary session in Washington on October 29 and 30 to expand its mandate for combating terrorist financing.

On the economic impact, the Group of Seven statement noted that the September 11 attacks “could delay the resumption of strong growth in our economies...”

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The full text of News Brief No. 01/98 is available on the IMF’s website (www.imf.org).
[but], notwithstanding remaining short-term uncertainties, we are confident about our future prospects. We are strongly committed to bringing forward needed measures to increase economic growth and preserve the health of our financial markets. We will continue to monitor exchange markets closely and cooperate as appropriate.

Turning to the prospects for emerging market and developing economies, which have already felt the effects of the slowdown of economic activity in the industrial economies, ministers and governors said these countries could be affected by the uncertainty following last month’s attacks, and the prospects of the poorest countries could be damaged. However, ministers and governors pledged to take all necessary steps to mitigate these effects. They also urged countries adversely affected by recent developments to create the conditions for strong economic growth and sustained private capital flows. “The international financial institutions,” the statement said, “stand ready to assist.”

On global integration and linkages among the world’s people, the Group of Seven officials said increased productivity growth and a higher rate of potential growth are key to raising living standards and reducing poverty. They pledged to do so by “promoting free trade and regulatory reform, strengthened capital markets, and enhanced educational opportunity.”

Noting that greater economic integration calls for increased international cooperation to support sound governance and strong institutions, the statement said “we will continue to take steps to address dislocations associated with economic adjustment and work to ensure that all can benefit from integration, including through well-targeted and well-coordinated development assistance, effective implementation of the HIPC [Heavily Indebted Poor Countries] Initiative, and poverty reduction strategies.”

Ministers and governors welcomed Russia’s continued economic growth, progress on reform, and ratification of new anti-money laundering legislation.


**Group of Seven economic leaders issue plan to combat financing of terrorism**

The following are extracts from the Action Plan to Combat the Financing of Terrorism issued on October 6. The full text is available on the U.S. Treasury Department’s website at www.treas.gov/press/releases/po667.htm.

We, the Group of Seven finance ministers, have developed an integrated, comprehensive action plan to block the assets of terrorists and their associates. We pledge to work together to deliver real results in combating the scourge of the financing of terrorism.

More vigorous implementation of international sanctions is critical to cut off the financing of terrorism. We are implementing UN Security Council Resolutions 1333 and 1373 [see related story, page 329], which call on all states to freeze the funds and financial assets not only of the terrorist Osama bin Laden and his associates, but of terrorists all over the world. Each of us will ratify the UN Convention on the Suppression of Terrorist Financing as soon as possible. We will work within our governments to consider additional measures and share lists of terrorists as necessary to ensure that the entire network of terrorist financing is addressed.

The Financial Action Task Force (FATF) should play a vital role in fighting the financing of terrorism. At its extraordinary plenary meeting in Washington, DC, FATF should focus on specific measures to combat terrorist financing, including:

- issuing special FATF recommendations and revising the FATF 40 Recommendations to take into account the

need to fight terrorist financing, including through increased transparency;

- issuing special guidance for financial institutions on practices associated with the financing of terrorism that warrant further action on the part of affected institutions and developing a process to identify jurisdictions that facilitate terrorist financing and making recommendations for actions to achieve cooperation from such countries.

Enhanced sharing of information among financial intelligence units is also critical to cut off the flow of resources to terrorist organizations and their associates. We call on all countries to establish functional financial intelligence units as soon as possible.

Financial supervisors and regulators around the world will need to redouble their efforts to strengthen their financial sectors to ensure that they are not abused by terrorists. We welcome the guidance by the Basel Committee on Banking Supervision on customer identification to stop the abuse of the financial system by terrorists and urge that it be incorporated into banks’ internal safeguards. We urge the IMF to accelerate its efforts, in close relation with the Financial Stability Forum [established by the Group of Seven to promote international financial stability through information exchange and international cooperation in financial supervision and surveillance], to assess the adequacy of supervision in offshore financial centers and provide the necessary technical assistance to strengthen their integrity.

We ask all governments to join us in denying terrorists access to the resources that are needed to carry out evil acts.
United Nations takes steps to eliminate international terrorism

Over the past several years, the United Nations (UN) has established 12 treaties and protocols on international terrorism. The first was signed in 1963 and the most recent, in 1999. Following the September 11 terrorist attacks, the Secretary-General called on member states to make it their “first order of business” to sign and ratify all UN treaties and protocols on international terrorism and strive to forge an agreement on a comprehensive convention against international terrorism, which is currently being discussed in the UN.

Freezing terrorist funds
The Security Council adopted a far-reaching anti-terrorism resolution (1373) on September 28, 2001, which legally binds the 189 UN member states to seek out and prosecute terrorists and halt all funds that support them. The resolution calls for the financial assets of those who commit, attempt to commit, or facilitate terrorist acts to be frozen. States should refrain from providing support to people involved in terrorism and prohibit their nationals or people in their territories from making funds or services available to terrorists.

Member states should also bring to justice anyone who has participated in terrorism or the financing of terrorist acts and ensure that such acts are established as serious criminal offenses in domestic laws and punished accordingly. Moreover, states should collaborate in criminal investigations and proceedings relating to the financing or support of terrorist acts.

The Security Council noted with concern the close connection between international terrorism and transnational organized crime, illicit drugs, money laundering, and illegal movement of nuclear, chemical, biological, and other deadly materials. It emphasized the need to simultaneously enhance coordination of efforts on national, regional, and international levels to strengthen the global response.

Finally, the Security Council decided to establish a committee (consisting of its 15 members) to monitor implementation of the resolution with the assistance of appropriate expertise and called upon member states to report within 90 days on the steps they have taken to implement the resolution. The committee is to submit a work program within 30 days of the adoption of the resolution and consider the support it requires in consultation with the Secretary-General. The ranking U.K. diplomat at the UN, Jeremy Greenstock, was named chair of the committee.

Measures to combat terrorism
In a week-long debate (October 1–5) in the UN General Assembly, member states from across the globe strongly condemned the menace of international terrorism while pledging to take specific and resolute steps to eradicate it. Addressing the General Assembly before the debate, New York City Mayor Rudolph Giuliani argued that this is not a time for further study or vague directives. The UN must hold accountable any country that supports or condones terrorism; otherwise, he added, it will fail in its primary mission as peacekeeper.

The Secretary-General stressed that terrorism will be defeated only if the international community summons the will to unite and that the UN is uniquely positioned to serve as the forum for this coalition.

Several speakers called attention to the need to define terrorism in order to effectively combat it. Others called for objective criteria that would allow the international community to identify and combat terrorism.

Many speakers called for adherence to existing UN antiterrorism treaties as well as the elaboration of new legal instruments to fight the menace. It was noted that the international community must work to ensure the universal adoption and full implementation of the existing counterterrorism conventions, while redoubling its efforts to conclude negotiations on the draft comprehensive terrorism convention.

A number of speakers also stressed the importance of cooperation on the regional and subregional level in the fight against terrorism.

Looking forward
It has not yet been determined how work in the UN will be coordinated with efforts in other forums to maximize the total impact of new and existing instruments in the fight against terrorism in general and its financing in particular. The Group of Seven Action Plan to combat terrorist financing (see page 328), which pledges to implement Security Council

<table>
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<tr>
<th>Members’ use of IMF credit (million SDRs)</th>
<th>During September 2001</th>
<th>January–September 2001</th>
<th>January–September 2000</th>
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<td>PRGF</td>
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<tr>
<td><strong>Total</strong></td>
<td><strong>9,472.97</strong></td>
<td><strong>21,801.82</strong></td>
<td><strong>3,177.63</strong></td>
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</table>

SRF = Supplemental Reserve Facility
EFF = Extended Fund Facility
CFF = Compensatory Financing Facility
PRGF = Poverty Reduction and Growth Facility

Figures may not add to totals shown owing to rounding.
Data: IMF Treasurer’s Department
Resolution 1373 and ratify the UN Convention for the Suppression of the Financing of Terrorism, is a step in the right direction. The envisaged revision of the Organization for Economic Cooperation and Development’s (OECD) Financial Action Task Force recommendations (FATF 40 Recommendations) should contribute to making the international legal framework more operational.

Finally, the proposed collaboration between the IMF and the Financial Stability Forum in assessing the adequacy of supervision in offshore financial centers and the provision of technical assistance to strengthen their integrity could help close existing loopholes and sustain future progress.

A xel Palmason
IMF United Nations Office

Stand-By, EFF, and PRGF Arrangements as of September 30

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<tr>
<th>Member</th>
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<th>Expiration date</th>
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<th>Undrawn balance (million SDRs)</th>
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1 Includes amounts under Supplemental Reserve Facility.
EFF = Extended Fund Facility.
PRGF = Poverty Reduction and Growth Facility.
Figures may not add to totals owing to rounding.
Data: IMF Treasurer's Department

Extended Fund Facility Arrangements are designed to rectify balance of payments problems that stem from structural problems.
The years 1979–89 were witness to a dramatic transformation both of the world economy and of the IMF’s role in the new order. In Silent Revolution: The International Monetary Fund, 1979–1989—the fourth in a series of official histories of the IMF—James Boughton covers both the political and the economic developments of this tumultuous decade. Boughton, who is currently Assistant Director of the IMF’s Policy Development and Review Department, was the IMF’s Historian from 1992 to 2000. Previously, he was an Advisor in the IMF’s Research Department. Boughton recently spoke with the IMF Survey about the latest history.

IMF Survey: The first question is prompted by the title of the new history: why do you call it the Silent Revolution?

Boughton: The impetus for the title was the speech that Michel Camdessus gave in 1989 in which he said there was, in his view, a silent revolution going on in the developing countries. What he meant by that was that country after country in the developing world were trying to reformulate their economic policies in a way that was market friendly, brought them into the world economy, moved away from a strong development role for the state, and enabled private sectors to develop. He called it a “silent revolution” because, to the naked eye, there was nothing very dramatic going on, but the effect on the world economy and on these particular countries was dramatic. So when I then looked at the whole time span, I said: “How did the world change?” If you took two snapshots—one in 1979 and one in 1989—you’d find the world had changed dramatically. Mexico is a good microcosm of what was going on in those 10 years. If you read what Mexican officials were saying in the late 1970s and early 1980s about how they thought their economy should be run and then you looked at what they were saying in 1989—it’s completely night and day.

IMF Survey: After the breakdown of the Bretton Woods system in the early 1970s, many observers said the IMF was really an institution that had lost its role. But you chart an extremely active and, at times, controversial period in the IMF’s history. What were the forces that drew the IMF into deeper involvement in the world economy?

Boughton: One thing I realized fairly early on in doing my research was that 1982 was really a bigger watershed year for the IMF than 1973 was. Most people—if they reflect on the history of the IMF and its 55 years of experience—think that 1973 was the big shift. Until then we had been overseeing the fixed exchange rate system; after that, we kind of drifted and had to look for a new role. But that’s not actually what happened. It’s true that 1973 drew the IMF into a more active and important role in the world economy than it had before, in the sense that the world was a less stable place. We had the oil shocks of the early and late 1970s, and we had all these floating exchange rates and countries having to develop their own exchange rate policies. The world needed a guiding force to cope with this new kind of rapid growth and greater instability.

What happened in 1982 was that all of those forces came to a head. Suddenly, a lot of countries were facing massive problems all at once, and this became the debt crisis. There was a great need for an agency to jump in and try to lead the world out of the crisis, to try to find solutions to those problems. And that agency turned out to be the IMF.

IMF Survey: Since 1979, no industrial country has borrowed from the IMF, and IMF lending has been entirely to developing countries. What effect has this change in lending had on the institution and its operations? Should the IMF become more involved in structural reform and longer-term lending?

Boughton: Certainly the demand for IMF resources shifted very dramatically. In the late 1970s, the IMF was still lending to the United Kingdom and Italy, and it was not at all obvious that the future of the IMF would be with the developing countries. But the rapid growth in private international financial markets, which started in the mid-1970s and became much more important in the 1980s and 1990s, insulated the industrial countries from the need for any financing from the IMF. That actually increased rather than
IMF Survey: During the 1980s, private capital flows became increasingly important, as they continue to be today. Has the development of private capital flows reduced the importance of the IMF as a source of official financing?

Boughton: I think it’s been quite the opposite. The growth of private markets has benefited a number of countries, but in many cases, only temporarily, or has benefited some countries one year and other countries the next. There was a huge inflow of private capital flows to emerging markets in the early 1990s, but when some of them got into trouble in the mid-1990s, the money simply vanished, and countries that thought they could rely on private markets found there would still be times when they would need official financing and that the IMF was an effective agency for filling those gaps.

IMF Survey: The IMF is now intimately involved in providing financial assistance to the poorest countries. What progress have you seen in this area since the early 1980s?

Boughton: This is probably the most controversial area for the IMF. It’s quite clear that the whole process of trying to provide stable long-term development financing, at least right now, could not work without the IMF being heavily involved, because the IMF is the only institution that has the credibility to impose effective policy conditionality. It’s the linchpin for making this whole process work.

Whether that’s the right long-run solution is another matter. Would the world be better off with one institution rather than several institutions providing coordinated financing and the right policy advice to poor countries? I don’t think we know the answer to that yet. Certainly in the 1980s, the IMF made huge progress toward developing a rational strategy for helping the low-income countries; for example, it established the Structural Adjustment Facility and then the Enhanced Structural Adjustment Facility, and there was steady progress from the mid-1980s to the late 1990s. But in my view, if we’re really going to see an effective mechanism for financing development in low-income countries, a lot more progress is needed.

IMF Survey: What conclusions do you draw from your work on the history, and what did you find that particularly surprised you?

Boughton: One main conclusion—and it’s kind of middle of the road—is that markets and institutions go hand in hand, that we need market-friendly solutions, but we need market-friendly solutions that are guided by institutions. We need both a visible hand and an invisible hand. I think that conclusion emerges whether you’re looking at the outcome of the debt crisis or whether you’re looking at financing for low-income countries.

As I was writing this book, I was fully aware that all the sources I was using would be accessible to other people interested in writing about the IMF.

—James Boughton

October 22, 2001

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The biggest surprise for me was that the 1980s turned out to be quite different from what I thought they were when I first started working on the book in 1992. I thought I was going to be writing about the last period when the IMF’s primary activity was providing balance of payments financing to its member countries. The 1990s were supposed to be a whole new ball game: the Soviet Union had collapsed, and the IMF was getting involved in transition issues as countries moved from central planning to markets.

What became obvious by 1998 when I essentially finished drafting the book was that the 1980s had set the stage for the IMF to play a very active and major role in emerging markets in the 1990s; that the role the IMF played in Mexico in 1995 and in Thailand, Indonesia, and Korea in 1997 and 1998 was made possible by its having been involved with emerging markets all through the 1980s. By becoming the major player in developing a strategy for dealing with the debt crisis in the 1980s, the IMF positioned itself for helping countries solve the problems of the 1990s. So, the whole dynamic changed from the time I started working on this project to the time I ended it.

**IMF Survey:** How would you distinguish the style and content of your history from earlier IMF histories? In this age of transparency, I’m sure there are materials you could bring in that previous historians maybe were not able to.

**Boughton:** The IMF is a very different place now from what it was when the previous histories were published. The first IMF history was written in the late 1960s, and the history previous to this one was written in the early 1980s. The IMF is now a much more transparent place. My predecessors had full access to the IMF archives; but they were the only ones who had such access. As I was writing this book, I was fully aware that all the sources I was using would be accessible to other people interested in writing about the IMF or about its member countries. So I’ve provided thousands of footnotes to internal IMF documents; people can now look at these footnotes and if they want to know more about a document, they can go look at it themselves.

Beyond that, I’ve tried to make this as much a history of the world economy in the 1980s as it is a history of the institution. All through the 1980s, the IMF was dealing with political issues as much as with economic issues; for example, several of the countries that were hit hardest by the debt crisis were also moving from military dictatorships to democracy. Argentina and Brazil provide clear examples. These countries were struggling with the need to establish democracy at the same time they were dealing with severe economic problems. And the IMF had to take all that into account. Dealing with political issues was unavoidable when the IMF was working with countries like Sudan, what was then called Zaire, Sierra Leone, and Liberia. All these countries had huge political and economic problems. All these political and economic issues overlapped, and the IMF had to come to grips with that. So this history is much more of a story about political economy than about technical economics.

**IMF Survey:** What will be the scope of the next chapter in the IMF’s history?

**Boughton:** As exciting as the 1980s were for the IMF, the 1990s were even more challenging and exciting. When you think about all the important stories of the 1990s—the geopolitical importance of Russia and all the work the IMF has done there; the financial crises; globalization—the history of the 1990s will be a fascinating story.
How can civil service reforms in programs supported by the World Bank and the IMF, particularly in low-income countries, be made more effective? On September 6, the IMF's Fiscal Affairs Department and the Public Sector Group of the World Bank's Poverty Reduction and Economic Management Network cosponsored a workshop on civil service reform with the goal of reaching a consensus on this question. This workshop was the second thematic discussion held in the context of strengthening the two institutions' collaboration on country programs and streamlining conditionality. About 60 staff, including managers and country teams from the Bank and the IMF, participated. The first workshop, held in July, focused on privatization of public enterprises.

In her opening remarks, Teresa Ter-Minassian, Director of the IMF Fiscal Affairs Department, noted the limited success of civil service reform. According to an IMF evaluation of Structural Adjustment Facility and Enhanced Structural Adjustment Facility programs during 1985–95, some wage bill reductions were obtained in the short run, but insufficient emphasis on strengthening institutions made it difficult to sustain employment and wage reductions. Cheryl Gray, Director of the World Bank's Public Sector Group, emphasized that civil service reform is crucial for improving governance and reducing poverty and that there is scope for strengthened collaboration between the Bank and the IMF to ensure consistency between the sometimes conflicting goals of short-term fiscal discipline and longer-term structural reforms.

Challenges of civil service reform
In the first session, participants discussed the motivation for civil service reform. The purpose of such reform is to ensure that payments for wages and pensions do not create fiscal imbalances and that incentives for civil service workers are adequate to ensure efficient service and good governance. In general, Sanjeev Gupta (IMF, Fiscal Affairs Department) noted, IMF-supported programs have assigned high importance to the wage bill and pension payments to ensure macroeconomic stability and sustainability. This was the case in Bank-supported programs as well. The difficulty with this emphasis is that it ignores structural objectives and fails to set priorities in the medium term, he said. Mike Stevens (World Bank, Africa Region) noted that there is no blueprint for civil service reforms because each country may require a different sequencing of reforms.

Participants generally stressed the need to better understand the political environment in which reforms are designed. In particular, Barbara Nunberg (World Bank, East Asia Region) observed that, in many cases, governments have been unable to resist pressures to increase wages or to provide employment as a social safety net to some segments of the population. Yasuiko Matsuda (World Bank, Latin America and the Caribbean Region) and Amit Mukherjee (World Bank, Europe and Central Asia Region) pointed out that the public often supports the demands of underpaid civil servants for higher wages and does not support civil service reform. Cyril Briançon (IMF, African Department) noted that strong labor unions may make it difficult to change wage and employment practices. Furthermore, insufficient “country ownership” of reforms has delayed the implementation of policies and therefore reduced the effectiveness of the reforms.

In summarizing the challenges, Helen Sutch (World Bank, Public Sector Group), who chaired the session, stressed that civil service reforms must be justified to policymakers and the public on the basis of their impact on poverty and on the effectiveness of government.

Bank and IMF approaches
The second session, chaired by Ke-young Chu (Deputy Director of the IMF's Fiscal Affairs Department), examined civil service reform in Bank- and IMF-supported programs. Describing how long it took for such reforms to bear fruit, Brian Levy (World Bank, Africa Region) pointed to Tanzania, where the current success took 10 years to achieve.

In the discussion, Valerie Mercer-Blackman (IMF, Western Hemisphere Department) noted that the timing of reforms is critical in some IMF-supported programs. Participants generally agreed that the timing and sequencing of reforms in Bank- and IMF-supported programs have sometimes been in conflict, in part because of differences in time horizons in the programs they support. In some cases, the need to reduce government spending has run counter to long-term structural reforms, such as the need to decompress wages and improve pay structures. Unless resolved, differences in strategy between the two institutions can reemerge as conflicts of timing.

Participants agreed that advice should be given in the context of a medium-term framework in order to assess all aspects of civil service reform and emphasized the need for early and frequent dialogue between the two institutions. Chu stressed that the macroeconomic and the structural components of civil service reform are inseparable and called for improved collaboration between the two institutions, particularly in light of the greater expertise of the World Bank in this area.
Conditionality

With regard to IMF conditionality, some participants questioned whether the IMF should impose conditions on civil service reform at all. In some cases, they argued, the wage bill may be the main fiscal problem, which would require that the IMF include conditionality to ensure that reforms actually take place. Moreover, according to Barbara Nunberg, IMF conditionality on short-term fiscal problems can lead to opportunities for longer-term reform and, in some cases, is critical in bringing about a consensus for reform. Nonetheless, in light of the track record with civil service reform to date, the sense of the meeting was that it was important that conditionality on future civil service reform be more selective and more sharply focused, with the Bank taking the lead on structural conditionality. Participants agreed that, to optimize Bank-IMF conditionality, care should be taken to ensure that the reforms programs are consistent.

Toward consensus

Chairing the final session, Gupta solicited participants’ views of the extent to which civil service reforms could be embedded, at least for low-income countries, in the poverty reduction strategy paper (PRSP) process. Claudia Costin (World Bank, Latin America and the Caribbean Region) emphasized the importance of engaging stakeholders early, being open about the strategy, and using high-quality data on employment and wages in formulating a reform strategy. For such a strategy to be implemented, the sequencing of civil service reforms needs to be tailored to each country’s circumstances. Nick Manning (World Bank Public Sector Group) noted the need for data on wage structures and sector-specific information that could be used to model the various reform scenarios. Participants also discussed various examples of countries in which data availability helped define the need for reform and convincingly the population of its benefits.

Summary and conclusions

Participants reached consensus on several key issues. First, they agreed that the staffs of the Bank and the IMF should engage in early dialogue during the implementation of civil service reforms in programs supported by the two institutions and should make the objectives of the reforms explicit from the outset. Second, the workshop concluded that short-run objectives—aimed at protecting the macroeconomic framework—and long-run objectives—linked to structural reforms—should be set in a medium-term fiscal framework, within which the fiscal impact of reform measures can be incorporated. Third, explicit recognition of the political challenges of reform is crucial. Fourth, conditionalities should be used sparingly. Consistent with the lead agency concept, the Bank would normally take the lead in advising on medium-term structural reforms and in designing conditionalities. Fifth, explicit discussion between the Bank, the IMF, and the government on timing and sequencing of reforms should precede decisions on key actions, such as civil service censuses, functional reviews, design of retrenchment programs, or monetization and consolidation of benefits. Sixth, national ownership is critical for the success of civil service reform. A first step in ensuring national ownership could involve identifying stakeholders and discussing with them what the trade-offs, in terms of public sector provision and tax burden, would be in the absence of reforms. In low-income countries, this discussion could take place in the context of the PRSP process. Finally, further efforts are needed to identify the core data that are needed to support civil service reforms and, in particular, to model different reform alternatives.

To build on the findings of the workshop, Teresa Minassian and Cheryl Gray agreed that the Bank and the IMF would select a group of focus countries to begin enhanced collaboration in the area of civil service reform. Bank and IMF staff working on these focus countries would agree on the priority macroeconomic, structural, and governance objectives for civil service reform, taking into account the medium-term fiscal framework within which these reforms must take place. In addition, country teams will agree on the sequencing of reforms, conditionalities, and the core data to support the reforms.

Selected IMF rates

<table>
<thead>
<tr>
<th>Week beginning</th>
<th>SDR interest rate</th>
<th>Rate of remuneration</th>
<th>Rate of charge</th>
</tr>
</thead>
<tbody>
<tr>
<td>October 8</td>
<td>2.55</td>
<td>2.55</td>
<td>3.00</td>
</tr>
<tr>
<td>October 15</td>
<td>2.60</td>
<td>2.60</td>
<td>3.06</td>
</tr>
</tbody>
</table>

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

Photo credits: Denio Zara, Padraic Hughes, Pedro Márquez, and Michael Spilotro for the IMF, pages 325–326, and 331–335; and Paul J. Richards for AFP page 327.
In addition to providing a twice-yearly survey of global prospects and policies, the IMF's World Economic Outlook includes analyses of selected topics of particular significance or interest. The recently published October 2001 World Economic Outlook takes an in-depth look at the information technology (IT) revolution. Although discussion of this important topic has been overshadowed by recent events (see IMF Survey, October 8, page 309), it is certainly a major development in the global economy, affecting all countries at all levels of development.

Although spending on IT (which the World Economic Outlook defines as “computers, computer software, and telecommunications equipment”) is likely to remain weak in the immediate future, according to the IMF study, as past overinvestment unwinds, the longer-term benefits for the global economy are likely to continue, or even accelerate, in the years to come.

Summing up its findings, the World Economic Outlook notes that, to date the IT revolution has largely followed the pattern of past technological revolutions, including an initial phase characterized by a boom and bust in the stock prices of innovating firms, as well as in spending on goods embodying the new technology. The IT revolution is different from past technological revolutions, however, in the globalization of production, which has strengthened real and financial linkages across countries. The rapid growth in the production of IT goods implies that changes in global demand conditions, driven mainly by IT-using advanced economies, have a significant impact on the exports of IT-producing countries. While positive demand shocks helped to boost IT production in 1999 and 2000, the current slump in global IT spending is a heavy drag on these IT-producing countries.

Notwithstanding the adverse impact of the current IT slump on some countries, the economic benefits of the IT revolution are already significant and will likely continue. Thus far, the benefits arise mainly from the fall in the relative prices of semiconductors and computers and accrue primarily to the users of these products. There is evidence that total factor productivity growth in IT production and IT-related capital deepening have boosted labor productivity growth in some countries, and it is likely that—in the coming years—economic activities in a variety of countries will be increasingly reorganized to take advantage of IT, yielding further benefits. The fall in relative prices of IT goods has also led to significant increases in consumer surpluses in IT-using countries.

Over the near term, despite the relatively rapid diffusion of the technology around the globe, the IT revolution is likely to benefit advanced countries more than developing countries. In the long run, however, the distribution of benefits will depend on specific country characteristics rather than relative incomes.

The IT revolution has important policy implications. Structural policies should encourage the widespread adoption and effective use of IT, including by promoting flexible labor markets and efficient service sectors. Uncertainty about the precise magnitude and likely duration of the acceleration in productivity implies that poli-
cymakers should place less weight on variables about which uncertainty has increased, such as the output gap, and more weight on observable variables, like actual inflation and a wide array of indicators of future inflation.
Over the past three to four years, Grenada, a member of the Caribbean Community (CARICOM) and the Eastern Caribbean Currency Union (ECCU), has been one of the fastest growing of the member countries of CARICOM (see chart, this page). Its success has been largely due to determined efforts aimed at strengthening the economy and diversifying its export product base.

**Economic developments**

The factors behind Grenada’s recent economic performance may be traced to the economic programs undertaken by the authorities beginning in 1992, aimed at breaking the cycles of slow growth and fiscal weakness that characterized much of the 1980s. The main objectives of the programs were to speed up the pace of growth, lower unemployment, and reduce poverty by promoting private sector investment in tourism and nontraditional sectors, improving roads and other infrastructure, and making the public sector leaner and more efficient. Private investment would be stimulated through the existing regime of fiscal incentives—mainly for manufacturing and tourism—that is common throughout the ECCU, a simplification of regulations governing investment, and reforms that lower tax rates and simplify the tax structure while broadening the tax base. The strategy to promote private investment also included the sale of the major state enterprises, including the electricity, telecommunications, and sugar companies; the privatization of the state-owned banks; and the contracting out of selected government activities, such as road construction and maintenance.

Public sector reforms focused on increasing fiscal saving through a reduction in the size of the civil service and a temporary wage freeze, and efforts to link pay more closely to performance. Grenada expected to alleviate a high incidence of unemployment and poverty—which stood at about one-third of the population at end-1992—through faster rates of economic growth. In addition, the economic programs undertaken by the authorities also incorporated more specific antipoverty measures, including an increase in spending on programs aimed at ensuring the basic minimum needs for young children, the aged, and the disabled.

Indications that the measures were bearing fruit began to appear in the mid-1990s. Real GDP growth rose from an average of close to zero in 1992–93 to 3 percent in 1995–96 and 7 1/2 percent in 1998–99, before falling back to 6 1/2 percent in 2000. Also, unemployment fell to 12 percent in 2000, and inflation remained in the low single digits, largely owing to the

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**Grenada: a small island economy**

Grenada comprises three small islands in the eastern Caribbean, with a total land area of 345 square kilometers and a population of some 102,000. The country is a member of the Caribbean Community (CARICOM), and the Eastern Caribbean Currency Union (ECCU) (see box, page 339). Banana cultivation and exports, the main economic activity until the early 1990s, declined rapidly during the middle of the decade and virtually ceased in 1997 as a result of low productivity and poor fruit quality, disease, and uncertainty regarding access to preferential markets in the European Community. The country remains heavily dependent on tourism and spices. In recent years, however, it has been able to weather the effects of the collapse of the banana industry by successfully diversifying into light manufacturing, offshore financial services, and—lately—telephone and Internet-based marketing.
fixed peg to the U.S. dollar. Growth was broad-based, with manufacturing (mainly electronic components and paper products), residential and hotel construction, and other services (particularly telecommunications and financial services) registering strong advances. This development, combined with high export prices for spices, led to an increase in GDP per capita from $2,650 in 1991 to almost $4,000 at end-2000 (see table, page 340).

A key feature of the recovery was the marked improvement in Grenada’s fiscal performance (see chart, this page). Government savings, which were negative during 1990–94, rose to 6 percent of GDP in 2000, reflecting strong economic activity, improved tax and customs administration, and measures to contain expenditure, particularly the wage bill, which fell from 13 percent of GDP in 1990–94 to 10 percent of GDP in 2000. The strengthened savings performance permitted increased capital spending (from 7 percent of GDP in 1990–94 to 11 percent in 1998–2000). Much of this spending centered on improving the country’s road network and sea defenses. Other large projects included the construction of government office buildings and a sports stadium, financed by commercial banks under lease-to-own arrangements. In the social area, the increased fiscal savings allowed increased transfers to small-scale rural projects, such as village roads, clinics, and water supplies, as well as higher direct payments to the poor.

**Prospects and challenges**

As in other countries in the Caribbean region, economic activity in Grenada is expected to slow in 2001, mainly because of the effects on the vital tourism sector of the slowdown of the U.S. economy that began to be felt in the first half of the year, and which were exacerbated by the September 11 attacks on the United States. (Tourism accounts for an estimated 25 percent of GDP, 40 percent of exports of goods and services, 9 percent of government revenue, and about 15 percent of total employment.) Initial estimates for 2001–02 indicate that the combined effects of these shocks would result in a sharp reduction in the growth rate and a worsening in the fiscal and external positions.

In response to the slowdown, earlier this year the government began to prepare contingency spending cuts, including a curtailment of large, domestically financed projects and of spending on goods and services. In addition, it will be important to take steps to contain the size of the wage bill, which accounts for about one-half of current expenditure. In line with the recent decision of the member countries of the Eastern Caribbean Central Bank (ECCB), the government has also undertaken to further strengthen revenue administration, including through the phasing out of some tax exemptions. These measures, together with the country’s ability to secure temporary financing because of its recent strong fiscal performance, should help Grenada weather most of the effects of the crisis.

Looking ahead, the challenge facing Grenada is how it can combine prudent fiscal policy with measures to sustain adequate rates of growth to reduce unemployment and alleviate poverty. Meeting these challenges will require building on the gains Grenada has achieved so far in reforming the economy and creating an environment that will continue to attract private investment and jobs. Prospects for growth still appear favorable based on ongoing and proposed tourist-related construction projects, proposals to expand the processing of spices and other agricultural products, and prospects for the further development of the telecommunications sector. In addition, the government remains confident that there is scope for promoting a well-regulated offshore financial services sector, though renewed efforts to strengthen regulation and to tackle money laundering are needed. While banana output has begun to recover under the government’s rehabilitation program, this sector is not likely to play a major new role in the economy, in part because of the continued uncertainty surrounding access and prices in export markets.

Maintaining a sound fiscal position will be essential for sustaining adequate growth rates and providing resources for further infrastructural and social programs without raising the debt burden. Proposals

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### ECCB region: central government current balance

(Percent of GDP)

![Graph showing current balance for ECCB region](image)

1 ECCB is the Eastern Caribbean Central Bank, whose member countries are Anguilla, Antigua and Barbuda, Dominica, Grenada, Montserrat, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines.

Data: Grenadian authorities; and IMF staff estimates.
on fiscal policy that are currently being discussed center on reducing tax exemptions, as part of a common regionwide effort; introducing a regional value-added sales tax; continued efforts to reduce the size of the civil service; and avoidance of commercial lease-to-own contracts to finance infrastructure projects, as part of a strategy to strengthen debt management and slow the growth of lease and interest payments. Early progress on the tax proposals is likely to be difficult, because their implementation requires a regional consensus, considerable preparation, and technical assistance.

Grenada’s economic performance since the mid-1990s, and, in particular, following the collapse of the banana industry in 1997, has demonstrated the country’s capacity to weather adverse shocks by adopting appropriate policies. The country’s ability to adapt its policies to deal with new external shocks will be severely tested as it takes steps to address the impact of the terrorist attacks on the United States. In these difficult circumstances, adhering to a strategy based on promoting investment, maintaining sound fiscal management, reforming the public sector, and alleviating poverty is likely to continue to serve Grenada well.

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### Available on the web (www.imf.org)

#### News Briefs

01/98: Statement of the Managing Director on the Situation of the World Economy and the Fund Response, October 5 (see page 325)
01/99: Uruguay: IMF Completes Second Review, October 5
01/10: Honduras: Completion (in principle) of Third Review Under PRGF, October 5
01/11: Rwanda: $12 Million Under PRGF, October 10
01/12: Press Statement by IMF Managing Director Horst Köhler on Meeting with Russian Leaders, October 12
01/13: IMF and Development Committee Meetings to Be Held November 17-18, 2001, in Ottawa, Canada, October 17 (see page 326)

#### Public Information Notices

01/10: Cape Verde, October 5
01/11: Equatorial Guinea, October 11

#### Letters of Intent and Memorandums of Economic and Financial Policies*

- **Mongolia, October 2**
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- **Cape Verde, October 10**
- **Rwanda, October 12**
- **Argentina, October 12**
- **Uruguay, October 12**
- **Assessments of Poverty Reduction Strategy Papers**
  - **Mongolia, October 2**
  - **Honduras, October 15**

#### Other

- **OECI Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, IMF Policy Development and Review Department, October 4**
- **IMF Financial Activities, October 5**
- **Update on the Financing of the IMF’s Participation in the PRGF and HIPC Initiative, October 5**
- **IMF Financial Activities, October 12**
- **Guidelines for Foreign Exchange Reserves, October 15**
- **Joint IMF-World Bank Staff Guidelines on PRSP Preparation Status Reports, October 15**
- **Tunisia: Observations of Interim Consultation Mission, October 15**

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