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In this issue

81
Horst Köhler nominated for IMF Managing Director

81
Conference debates data initiatives

85
IMF reviews Mozambique's needs

86
Ukraine review commissioned

87
Lessons from Japan's banking crisis

90
Poland: East Europe's 'tiger'

93
Stand-By approved for Argentina

94
Support package for Ecuador

95
Social spending rises under IMF programs

and . . .

89
New on the web

92
IMF Arrangements

93
Use of IMF credit

94
Recent publications

96
Selected IMF rates

Current EBRD President

IMF Executive Board receives nomination of Horst Köhler for Managing Director

On Tuesday, March 14, the IMF Executive Board received a formal nomination of Horst Köhler for the post of the Managing Director of the IMF.

Köhler, President of the European Bank for Reconstruction and Development (EBRD), was nominated on behalf of the European Union member states by Joao Santos, an Advisor in the Executive Board constituency that includes Portugal, which currently holds the presidency of the European Union. Bernd Esdar, Executive Director for Germany, made a statement in support of the nomination of Köhler (see page 82).

Horst Köhler

The Board was also informed of the withdrawal of Eisuke Sakakibara, former Vice Minister of Finance for International Affairs in the Ministry of Finance of Japan, as a candidate for the post of IMF Managing Director.

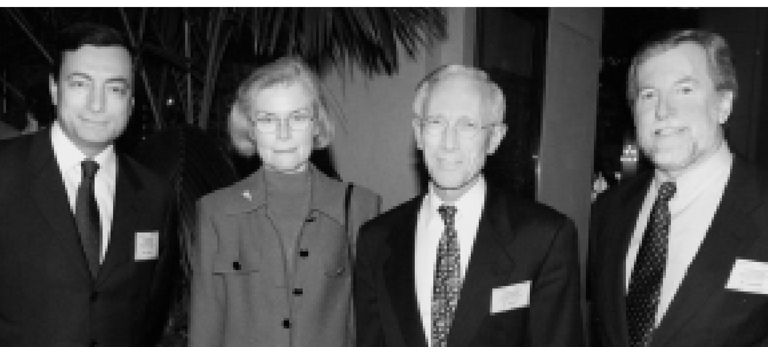
On Thursday, March 16, Jose Pedro de Morais, Jr., the Executive Director representing the constituency of African countries that include Angola, announced that he had withdrawn the nomination of Stanley Fischer, currently Acting IMF Managing Director, to the position *(Please turn to the following page)*

IMF–Financial Stability Forum conference

Data users and compilers search for consensus on statistics initiatives, resource implications

In an effort to reach greater consensus on data priorities, compilers and users gathered in Washington, D.C., on February 23–24 for the IMF Conference on Capital Flow and Debt Statistics. The event drew 120 senior officials from central banks, finance ministries, national statistical offices, the Bank for International Settlements (BIS), the IMF, and other international and regional agencies, as well as top-level participants from commercial banks and investment firms.

The conference, cosponsored by the Financial Stability Forum's Working Group on Capital Flows, was timed to complement an upcoming IMF Executive Board discussion of initiatives to strengthen the IMF's Special Data Dissemination Standard (SDDS) and General Data Dissemination System (GDDS) in the area of external debt and to provide wide-ranging commentary to the working group, which was finalizing its report on cross-border capital flows, external positions, and the analytical bases for risk and liquidity management.



At the conference (left to right): Mario Draghi, Carol Carson, Stanley Fischer, and Jack Boorman.

Participants emphasized the key role that better and more timely data can play in facilitating more knowledgeable market decisions and more effective policymaking. But the exchange of views also highlighted the resource constraints that face already overburdened national statistical offices. *(Continued on page 83)*

Köhler nominated for IMF Managing Director

(Continued from front page) of Managing Director, at Fischer's request. Fischer also issued a statement, excerpts of which follow:

"I was honored to have been nominated for the position of Managing Director of the International Monetary Fund by Mr. Jose Pedro de Morais, Jr., and by the support of other Executive Directors.

"In view of the emerging consensus behind the candidacy of Horst Köhler, President, European Bank for Reconstruction and Development, I have asked Mr. de Morais to withdraw my nomination. I am deeply grateful for the confidence he and his colleagues and the countries they represent have expressed in me.

"I had an excellent meeting this morning with Mr. Köhler, during which we discussed the challenges the IMF faces. I am confident that under his leadership the IMF will become an even more effective institution. I look forward to working closely with him, my colleagues in management and the staff, as well as the members of the IMF, as we move forward."

Köhler holds a doctorate in economics and political science from Tübingen University. He has been president of the EBRD since September 1998. Previous positions include president of the German Savings Bank Association and European Savings Bank Group from 1993 to 1998. He also served as Germany's Deputy Minister of Finance from 1990 to 1993, having previously held a number of posts at the Federal Ministry of Economics and the Federal Ministry of Finance from 1976 through 1989.

Following are edited excerpts of the statement by Bernd Esdar, Executive Director for Germany, nominating Horst Köhler.

Esdar statement

The government of Germany is grateful to the member states of the European Union for their unanimous expression of support in nominating Horst Köhler as their candidate for Managing Director of the IMF.

Mr. Köhler is eminently qualified to lead the IMF at the dawn of a new century.

As President of the EBRD, as president of the German Savings Bank Association, and as Germany's Deputy Minister of Finance, Mr. Köhler has performed with distinction, drawing the praise of the international community for his policy orientation, his strategic outlook, and his vigorous commitment to dialogue and partnership as the basis for successful international cooperation.

In 1990, he was appointed Deputy Minister of Finance, playing a central role in the process of political unification of Germany.

Most notable at this period is his work in the realm of international financial and monetary policy. He served as a Group of Seven Deputy and "sherpa" in the preparation of the world economic summits in Houston (1990), London (1991), Munich (1992) and Tokyo (1993). His wide knowledge and deep understanding of the complexities of reunification helped prepare the international community for the inclusion of Russia in the Group of Seven process.

As Deputy Minister, one of Mr. Köhler's duties was to formulate the German government's position on all issues of the operating policy of the IMF. Besides his duties in connection with the IMF, he also served as Deputy Governor at the World Bank and was intensely concerned with issues of development policy.

In August 1993, Mr. Köhler followed a call from the German Savings Bank Association to become its president. In this capacity, he initiated a structural change in this financial group to improve its competitiveness. But he also understood this group as contributing to a political concept and process for adjusting to globalization, while at the same time safeguarding economic and social stability at the local level.

In September 1998, with the unanimous backing of its shareholders, Mr. Köhler became president of the EBRD in London. He took over the institution in the immediate aftermath of the financial crisis in Russia. He orchestrated a cleanup of the project pipeline and a successful review of the EBRD's medium-term strategy and thus not only led it to profitability again but also strengthened it to better meet the transition challenges ahead.

During his EBRD presidency, he strongly advocated closer cooperation among the multilateral development banks and the IMF, with two pilot initiatives for enhanced cooperation (in Romania and the Kyrgyz Republic) launched last year.

Mr. Köhler knows the international financial world from all points of view. He is equally familiar with macroeconomic policy, structural adjustment and investment financing. Both crisis prevention and crisis management are among his strong suits, as is his ability as a good communicator. ■

The full text of Press Release Nos. 00/18 and 00/19, as well as nominating statements, Köhler's curriculum vitae, and statements by Fischer and Morais, is available on the IMF's website (www.imf.org).

Photo Credits: Denio Zara, Padraic Hughes, Michael Spilotro, and Pedro Márquez for the IMF, pages 81 and 83–84; Odd Anderson for AFP, page 85.

Data conference is forum for compilers, users

(Continued from front page) The conference represented an important first step in expanding the degree of understanding that compilers and users in the public and private sectors have of each other's needs. It helped delineate many of the critical issues before the statistical and policymaking communities, and frank exchanges helped clarify the differences in perspectives that shape user and compiler positions.

Overview

In his welcoming remarks, IMF Acting Managing Director Stanley Fischer noted that this conference represented a signal opportunity to improve understanding and coordination between data users and compilers. He asked attendees to consider a number of questions, including whether the push for improved data should not also encompass a press for greater resources for statistical operations and whether goals should be more clearly defined in the quest for better debtor and creditor data. On the debtor side, he asked participants to be mindful of the distinction between residents and nonresidents, look at both domestic and foreign debt, and address the question of reserves. From the creditor's perspective, the question remains how to interpret international banking statistics.

The resources brought to bear on these data issues will be enhanced, Fischer added, if international and national efforts are coordinated and if international organizations complement—not duplicate—their efforts. Good data play a key role in formulating effective policies and avoiding crises, he said, and that lesson was vividly in evidence for the IMF during the Asian crisis, where the absence of timely data allowed debt problems to fester until they reached crisis proportions.

Mario Draghi, Director General of the Italian Ministry of the Treasury and Chair of the Financial Stability Forum's Working Group on Capital Flows, briefed participants on the perspective his working group brought to these issues. He voiced concern that policymakers and market participants did not spend sufficient time communicating with one another and that data compilers were frequently not fully aware of users' requirements. Draghi said the conference was a good starting point for improved coordination, but he also pointed to the need for better coordination at the national level. Statistical offices needed to keep pace with the rapidly increasing sophistication of the international financial markets, he cautioned. Progress had been too slow in such central areas as compiling comprehensive data on short-term debt; filling gaps in information on offshore centers, derivatives, and other off-balance-sheet items; and addressing data discrepancies.

The task was admittedly an ambitious one, Draghi noted, but the price of inadequate data—in terms of market uncertainty and crises—was simply too high to be considered a viable alternative.

Why good data matter

One of the critical lessons of the past five years is that in a world of increasingly integrated capital markets, the importance of reliable and timely data—especially on external debt and capital flows—cannot be overestimated. This point was stressed by both Caroline Atkinson, Deputy Assistant Secretary for International Monetary and Financial Policy at the U.S. Treasury, and Nouriel Roubini, Director of the Policy Development and Review Department of the U.S. Treasury, in presentations that proved broadly reflective of the views of a wide range of data users.

Atkinson outlined the case for improved data, arguing that without solid information, policymakers simply operated blind. When there was bad news, countries might instinctively want to hide it, but markets had a way of imagining terrible things in a news vacuum, and this can precipitate a crisis. Greater transparency and better information, she said, form the core of the new financial architecture.

Roubini acknowledged the real constraints many statistical agencies confront but insisted that recent experience indicated that consistent, comparable, and analytically useful measures of external debt could serve as a modern equivalent of the canary in a coal mine—providing early warning of rising dangers and averting more costly problems down the line. He argued, in particular, for enhanced measures of liquidity risk and greater attention to balance sheet risk.

What price better data?

The IMF's SDDS and GDDS have provided a systematic structure for data dissemination in the global community, according to Paul Cheung, Chief Statistician of Singapore's Department of Statistics. In a presentation that struck a chord among a number of statistical compilers, he contended that the global community has bought into the concept of data dissemination standards because of their general applicability. But broad support for these initiatives might be jeopardized and lead to nonobservance or even withdrawal, Cheung cautioned, if proposed additions to the SDDS and GDDS were designed too specifically to address the problems of a subset of countries.

Cheung agreed, for example, that external debt issues could pose systemic risks but questioned the relevance of requiring quarterly external debt reporting from net creditor countries. Creditor countries, he explained, would have to divert scarce resources to meet this tight monitoring system and would have to make unnecessarily burdensome demands on respondents.

Caroline Atkinson

Nouriel Roubini

Paul Cheung

Annual data, he suggested, would suffice for net creditor countries. Some participants disagreed, noting that the distinction between debtor and creditor countries may be a fluid one and that even major industrial countries are subject to external debt problems.

Supplementary data

In addition to proposed improvements in core data, the conference examined whether other types of debtor information could usefully, and practically, be compiled. Paul Tucker, Deputy Director, Financial Stability, Bank of England, focused his remarks on national risk management, suggesting better information and analysis would be needed on financial derivatives, given their growing role, and that debt managers should make greater use of stress tests to gauge the impact of exchange or interest rate changes—for example, on balance sheets. He also suggested that the results of individual stress tests could be aggregated to an experimental measure of systemic stress. But he, too, acknowledged the limited resources available for data initiatives. Often, the data needed depends on the question being asked. For the United Kingdom, service sector data had become a priority, he said. Debtors, on the other hand, must prove themselves to creditors and are in a more natural position to need, and want, to collect external debt data.

Paul Tucker

Miki Eran, Controller of Foreign Exchange for Israel, outlined her country's experience, observing that some costs of data initiatives (for example, in exchange rate exposure) were more easily handled in a country such as Israel that had once had a system of exchange rate controls in place. The system set up to administer controls was adapted for new purposes, and the costs involved in new data gathering were kept in line by limiting the number of respondents (only "big players" were required to report), allowing respondents to choose the Internet or whatever reporting system suited their needs, and giving them the software needed to reply.

Miki Eran

Credit and market data

One means of closing gaps in external debt data is to make greater use of creditor and market sources of information. Philip Turner, Head of Secretariat, Emerging Markets, BIS, noted that his organization was considering changes on three fronts: measuring exposures on an "ultimate risk" basis (banks already assess their exposure in this fashion), working cooperatively with commercial banks (demonstrating why banks and other users need this data and ensuring that banks' reporting load remains reasonable), and enhancing the coverage and analytical usefulness of BIS data. Turner explained that the BIS was seeking to improve existing statistics (notably offshore reporting) and stood ready to facilitate the establishment of bilateral contacts between debtors and creditors to examine discrepancies between the two groups' data.

Philip Turner

Guillermo Le Fort, Director of International Affairs for the Central Bank of Chile, argued for a statistical system that differentiates assets and liabilities by their risk characteristics as well as by their functional classification. He underscored the importance of taking external assets into account in the analysis of vulnerability, cautioning that focusing only on liabilities could overstate vulnerabilities.

Guillermo Le Fort

High-frequency monitoring

Participants generally saw value in having some means of frequent monitoring of foreign external market activities and views, but differed on how this might be carried out. James Lau, Executive Director of the Hong Kong Monetary Authority, stressed that one-size solutions and universal templates were inappropriate for this purpose. The experience of Hong Kong SAR, he suggested, argued for some type of customization for small and medium-sized markets. While most countries engage in some sort of high-frequency monitoring, practices differ widely. Developing countries tend to rely more heavily on statistical reporting by market participants, while industrial countries place more reliance on informal contacts to elicit market views and expectations. In a complementary presentation, Dino Kos, Senior Vice President of the U.S. Federal Reserve Bank of New York, reviewed the United States' long experience with both formal and informal systems of high-frequency monitoring. For the United States, it is considered less important to know who is active in the market than why they are active.

James Lau

Dino Kos

Concluding observations

Broadly, the conference delineated two contrasting positions. Policymakers and data users (and a few compilers) argued forcefully for better—that is, fuller and more timely—data on capital flows and external debt. They cited the key role better information plays in shaping more effective policies and in facilitating more appropriate investment decisions. In contrast, compilers from industrial countries and off-

shore centers typically were more conscious of the multiple demands placed on national statistical resources and were less convinced of the value of providing such detailed and high-frequency data on external debt.

Compilers and users commended the beneficial role played by the SDDS and the GDDS, but expressed less unanimity on proposals to strengthen the external debt component of both. Participants vigorously debated the merits of requiring net creditor countries to submit more frequent debt data, and some questioned more broadly the practicality of a one-size-fits-all approach to the new data proposals.

There was widespread support for the continued improvement of the statistical frameworks being developed by international organizations and for other international cooperative efforts, such as the BIS's long-standing International Banking Statistics, the IMF's Coordinated Portfolio Investment Survey, and the Joint BIS-IMF-OECD-World Bank Statistics on External Debt. And there was unquestioned agreement on the value of developing and improving creditor data as well as wide recognition of the usefulness of attempting to reconcile debtor and creditor data as a way of improving national data.

While a number of participants forcefully made the case for exercising restraint in adding new categories of data, there was considerable concern about the increasing importance of nonbank private institutions and the relative absence of data on their activities. Among the ideas to improve the data on nonbank private institutions were proposals to encourage data disclosure for market use, improve transparency, employ new technologies to obtain data faster and more cheaply, and make wider use of existing databases maintained by private firms and regulatory agencies.

Virtually all participants acknowledged that data initiatives would impose growing demands on countries' statistical resources. Some worried about a diminution of quality; others advised making the best use of limited resources and finding a good solution when the ideal was out of reach.

In her summary, Carol Carson, Director of the IMF's Statistics Department, stressed the usefulness of "getting views on the table." The conference had highlighted the importance of perspective. She noted that a consensus between data users and data compilers on priorities for producing better data more quickly had not emerged. Data viewed as crucial at the global level may appear much less vital to national compilers. Resource constraints are real, and hard-pressed data compilers at the national level have yet to be convinced of the need for, and the urgency of, international data requests. The case for improved international data, Carson said, needs to be made more convincingly.

Jack Boorman, Director of the IMF's Policy Development and Review Department, acknowledged that the conference discussions had revealed "a lot of operational problems" for which quick or easy solutions were not readily available. For many international organizations, the recent crises in Asia and elsewhere—and the stunning absence of key data on a timely basis—had galvanized them to consider remedial action. There was clearly value in forums that brought users and compilers together, enhanced communication, and, ideally, laid the foundation for future consensus and action in these areas. Boorman indicated that since these efforts were not starting from scratch but were rather building on existing systems, progress was likely to come to a large extent through ad hoc improvements. But he was convinced that data collection and dissemination were improving and making a positive difference. ■

The agenda and background material prepared for the Conference on Capital Flow and Debt Statistics: Can We Get Better Data Faster? will be posted in late March on the IMF's website (www.imf.org).

IMF willing to augment credit to Mozambique

On March 3, the IMF Executive Board said it would consider augmenting Mozambique's access to the Poverty Reduction and Growth Facility (PRGF), given the economic impact of the recent devastating floods. The text of News Brief No. 00/12, which follows, is also available on the IMF's website (www.imf.org).

The IMF Executive Board noted that Mozambique had been hit over the past three weeks by its worst natural disaster on record. Directors expressed sympathy to Mozambique and its people for the heavy losses suffered in severe flooding.

Directors were willing to augment Mozambique's access to resources under the PRGF (see *IMF Survey*, July 5, 1999, page 221), given current conditions in the nation. Based on estimates of the economic impact of the floods and of the donor response so far to it, the forthcoming staff report for the PRGF review could include a proposal for higher access. At the same time, Directors expressed a desire to consider the PRGF review on an accelerated schedule.

Directors also considered the possibility of adjusting the delivery schedule for already agreed IMF assistance under the Heavily Indebted Poor Countries (HIPC) Initiative in such a way that, if combined with maximum interim relief under the enhanced HIPC Initiative, there would be very little, or possibly no, cash debt service payable to the IMF for about one year.

Photo not available

A woman carries water from a well in the town of Canicado, Mozambique.

News Brief

IMF responds to allegations about Ukraine's use of international reserves, outlines remedial actions

In a news brief dated March 14, the IMF noted that various allegations have been made about the use of Ukraine's foreign exchange reserves held by the National Bank of Ukraine (NBU) in 1996–98, before the approval of the current arrangement under the Extended Fund Facility (EFF) on September 4, 1998. Excerpts from News Brief No. 00/15 follow. The full text is available on the IMF's website (www.imf.org).

At the request of the IMF staff, Pricewaterhouse-Coopers (PwC) has been commissioned by the NBU to carry out a special examination of the transactions affecting the reserves in 1997–98. When completed, the results will be published. In the meantime, this statement sets out the IMF staff's current understanding of the transactions to which the allegations relate. It explains when the staff learned about the transactions and the remedial actions that have been taken.

In summary, on the basis of the information currently available to IMF staff, it appears that a number of transactions in 1996–98 gave the impression that Ukraine's reserves were larger than was actually the case. Relatively few of these transactions appear to have resulted in Ukraine's receiving disbursements that it would not otherwise have been entitled to receive. Pending the final results of PwC's special examination, the view of the IMF staff is that Ukraine appears to have received disbursements from the IMF on three occasions in late 1997 and early 1998 that it would not have done if the true state of Ukraine's reserves had been known at the time. The IMF will review this thoroughly when the results of the special examination are available. Since the approval of the subsequent arrangement for Ukraine under the EFF in September 1998, new safeguards have been put in place and there has been no evidence of similar problems.

In recent months, the IMF has been considering ways to strengthen safeguards on the use of IMF resources and also how best to address cases where national authorities misreport information to the IMF. It is anticipated that further safeguards will be adopted after the IMF Board has discussed this issue in the coming weeks.

Remedial actions

Since it became clear to IMF staff in August 1998 that part of the NBU's reserves were tied up, a number of actions have been taken under the current EFF arrangement to correct the situation. First, the NBU ensured that all its liquid reserves were held in first-rank international banks. Second, it allowed virtually all of the transactions that had rendered part of its reserves illiquid to unwind, and it undertook not to carry out similar transactions in the future. Third, it agreed that PwC would conduct quarterly audits of the reserve position of the NBU in the future. While PwC made a brief check on the end-September 1998 position, the first full quarterly audit was undertaken for the reserves at end-December 1998, when an additional transaction was revealed. Subsequent audits have not revealed any further transactions of this nature.

Under the EFF arrangement, the IMF staff has been monitoring the level of reserves daily to help ensure that they are liquid, and there has been no evidence of problems similar to those noted above. More specific targets have been set for liquid reserves, and decisions about IMF disbursements have related to performance compared with these targets.

No remedial action was taken following the revelation to the IMF staff in April 1999 of the $150 million round-tripping exercise in November 1997. At that time, the staff members concerned assumed that the formal requirements of the Stand-By Arrangement that was in place in August 1997 through August 1998 were not breached, and they knew that the transaction had been unwound in January 1998. However, it does now appear likely to the IMF staff that there was a breach of the requirements of the Stand-By Arrangement as a result of this transaction.

The NBU has initiated a special examination of all transactions above $20 million affecting the reserves between December 31, 1996, and September 30, 1998. The results covering the key period from July 31, 1997, to January 31, 1998, are expected by the end of March, and those for the rest of the period by the end of June. The NBU has implemented some improvements in reserve management practices and is discussing further changes with IMF staff. In the event any future disbursements from the IMF are approved, the Ukrainian authorities have agreed that they will voluntarily keep the proceeds in an account in the IMF. When the results of the special examination are available, the IMF will consider further remedial actions. ■

Correction

In the *IMF Survey* dated March 6, there was an error in the story on emerging markets. The next-to-last sentence on page 76 should have read: "The more complete such information is and the more widely disseminated, the better equipped the private sector is to make its own risk assessment and to decide how fully it wishes to participate."

Deregulation, weak corporate governance contributed to systemic problems

In the second half of the 1980s, Japan enjoyed above-trend economic growth and near-zero inflation. These conditions resulted in a significant decline in the country risk premium and a marked upward adjustment in growth expectations, which boosted asset price inflation fueled by credit expansion. At the time, Japanese banks were considered among the strongest in the world. During the same period, the pace of financial liberalization and deregulation accelerated, which spurred price competition and prompted banks and other depository institutions to take greater risks, including increased lending to the real estate industry. As land prices rose, these institutions loosened credit standards. In response, the authorities limited total bank lending to the real estate sector, curtailing the banks' asset growth.

Asset prices peaked in 1989 and collapsed after the summer of 1990. Economic growth subsequently slowed and, along with the decline in stock and real estate prices, weakened banks and other financial institutions. By 1997, Japan was in the midst of a full-blown banking crisis. An IMF Working Paper by Akihiro Kanaya and David Woo, *The Japanese Banking Crisis of the 1990s: Sources and Lessons*, examines what went wrong and why it has taken the system so long to recover.

The Japanese banking crisis is a fitting subject for a case study, the authors say. First, most of its underlying causes are typical of banking crises in general. Second, it serves as a warning that even a seemingly robust and relatively sophisticated financial system like Japan's is not immune to crisis. Third, it demonstrates that such a crisis can entail large costs for the country. In fact, according to Kanaya and Woo, a number of researchers attribute the stagnation of the Japanese economy in the 1990s in large part to the banking crisis.

What went wrong?

The working paper traces the problems in Japan's banking system to the increased pace of deregulation and a deepening of the capital markets in the late 1980s, which overburdened the capacity of the system. Financial liberalization and deregulation took the form of a relaxation of interest rate controls; capital market deregulation, which included measures that made it easier for large corporations to borrow directly from the market; and a relaxation of restrictions on the activities of institutions that had previously been tightly segregated. For example, agricultural, fishery, and credit cooperatives were allowed to increase their lending to nonmembers.

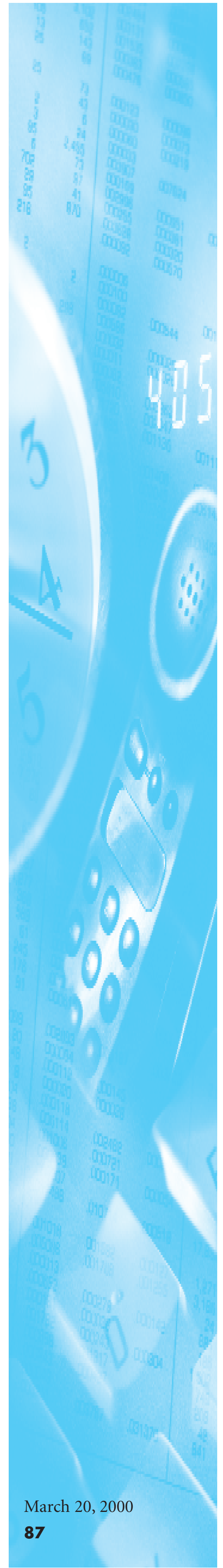
These developments, Kanaya and Woo observe, had important implications for banks and other depository institutions. Price competition intensified, eating into the banks' risk-adjusted interest rate margins. Banks reacted by taking on more risk, for example, extending the average maturity of their loans. To boost short-term profits, they loosened credit conditions.

The Japanese stock market peaked at the end of 1989. In April 1990, the authorities began to limit bank lending to the real estate sector in an effort to rein in land prices, which started to decline in 1992. As a result, Kanaya and Woo explain, the banks' asset growth began to level off, declining from ¥508 trillion in 1989 to about ¥491 trillion in 1990. The collapse of asset prices in 1990 caused economic growth to slow, significantly weakening the banks and other financial institutions. The weakening was manifested in the rapid deterioration of the quality of loans to the real estate industry, erosion of the value of collateral, mounting pressure on bank capital, and a decline in debtors' ability to continue servicing their loans.

Other developments that exerted pressure on banks, Kanaya and Woo observe, included their downgrading by credit-rating agencies, which began in 1989, and the gradual lifting of restrictions on Japanese corporations' access to the domestic and euro bond markets, leading to an acceleration of new bond issues (see table, page 87). The downgrading of Japanese banks made it more attractive for larger Japanese corporations—which by 1989 had unrestricted access to the capital market—to raise funds in the capital market than to borrow from banks whose credit rating was lower than theirs. The restrictions on small and medium-sized companies in the domestic market were gradually removed during the 1990s.

Why recovery was slow

Although some banks took steps to reinforce credit standards and conditions following the collapse of asset prices, this effort did not go far enough to jumpstart the recovery. Kanaya and Woo attribute the seriousness of the banking crisis, in part, to weak corporate governance. The ownership structure of a typical Japanese bank gives relatively few shareholders the majority of total outstanding shares. This has given rise, the authors say, to a "largely ineffectual corporate governance system in which shareholders have only a modest control over the management of banks." As a result, bank management is not pressured to maximize profitability, focusing instead on market share and on providing stable employment and services for clients. (Kanaya and Woo note that before interest rates were relaxed, Japanese



banks derived most of their income from interest earnings, so that their outstanding loans largely determined the size of their net income. Banks' preoccupation with market share is a legacy of this earlier system.)

Weak profitability, in turn, means that when loans go bad, banks do not have the retained earnings to deal with them and, moreover, have difficulty raising new capital in the market. In addition, with weak accountability, bank managers do not have the incentive to restructure and will not address problems during their tenure. Another feature of Japanese corporate governance, which Kanaya and Woo say had worked reasonably well until the 1990s, was a system in which lenders designated a main bank to act as monitor of the borrowing firm and mediator when borrowers experienced stress. The main banks were responsible for identifying problem borrowers before they became insolvent and for helping them restructure their businesses. Problems arose when the main banks themselves came under stress and, rather than allow their borrowers to default, treated them leniently despite their questionable long-term viability.

Credit rating of Japanese city banks

	Bank of Tokyo-Mitsubishi	Dai-Ichi Dangyo Bank	Fuji Bank	Sakura Bank	Sanwa	Sumitomo Bank	Tokai Bank
1980		B	A/B		B	A/B	B
1981		B	A/B		B	A/B	B
1982		B/C	A/B		B	A/B	B
1983		B/C	A/B		B	A/B	B
1984		B	B		A/B	A/B	B
1985		B	B		A/B	A/B	B/C
1986		B	B		B	B	B/C
1987		B	B		B	B	C
1988		B	B		B	B	B/C
1989		B	B		B	B	B/C
1990		B	B	B/C	B	B	B/C
1991		B	B	B/C	B	B	B/C
1992		B/C	B/C	B/C	B/C	B/C	B/C
1993		B/C	B/C	C	B/C	B/C	B/C
1994		B/C	B/C	C	B/C	B/C	B/C
1995		B/C	C	C/D	B/C	B/C	C
1996	B/C	C	C	D	C	C	C/D
1997	B/C	C	C/D	D	C	C	C/D
1998	C	D	D	D	C/D	C/D	D
1999	C/D	D	D	D	D	C/D	D

Data: IMF, *The Japanese Banking Crisis of the 1990s: Sources and Lessons*

Authorities' initial response

Between 1990 and 1995, Kanaya and Woo say, the authorities did little to address the deteriorating conditions in the banking system, partly because they held out hope that the economy would recover on its own and give the banks the boost they needed. Although the banks continued to deteriorate after 1995, the authorities were reluctant to intervene for fear of igniting a panic. Their reluctance, the authors explain, was compounded by the fact that Japan did not have an adequate deposit insurance scheme or a legal framework for dealing with a full-scale banking crisis. This regulatory "forbearance," Kanaya and Woo note, created moral hazard problems and further weakened the banks. Depositors had begun to withdraw their funds from weakened financial institutions in 1995 but, following the failures of several major ones, increased their withdrawals in 1997.

When the authorities finally intervened, they did so only after the affected banks became insolvent, and their delay prolonged the crisis. With the effective bankruptcy in 1997 of several large, high-profile institutions, the Japanese authorities ordered these institutions to suspend their operations. Subsequently, the authorities introduced a framework for dealing with banking crises. It gave banks the responsibility for valuing their assets according to well-defined guidelines and then required external review and monitoring of these findings. A second component of the framework was designed to narrow the scope for regulatory forbearance by defining conditions under which regulators would have to take remedial action against banks.

By 1998, the public recognized that the problems were severe enough to require public funds to restructure the system. Although emergency laws were passed in February 1998 to stabilize the financial system, Kanaya and Woo say the banking supervisory authorities were still not fully equipped to deal with the magnitude of the problem.

New framework

In June 1998, the Financial Supervisory Agency was established to take over bank supervision from the ministry of finance and was granted the independence to operate more effectively. In October, the Diet passed two laws—the Financial Revitalization Law and the Financial Early Strengthening Law—to help resolve banking problems. The Financial Revitalization Committee, established to oversee the bank restructuring process, required banks seeking a capital injection to submit a restructuring plan, which would be subject to review. At the same time, the Diet doubled the amount of funds earmarked for strengthening the banking sector, which made available ¥60 trillion (12 percent of GDP)—¥25 trillion to recapitalize weak but solvent banks, ¥18 trillion to nationalize or liquidate insolvent banks, and ¥17 trillion to fully protect the deposits of insolvent banks.

Although bank closures or suspensions continued during 1998, Kanaya and Woo say that the Japanese banking sector appears, for the time being, to have stabilized. They emphasize, however, that the sector's long-term health is still contingent on the banks' ability to restructure, which

will entail tackling still sizable problems with the quality of assets, dealing with weak corporate profitability, and strengthening corporate governance.

The authors describe three recent developments that—if they become a trend—bode well for the future of the Japanese banking system: voluntary mergers; approval of a foreign acquisition of a major Japanese bank, which would reinforce the introduction of modern banking practices in Japan; and a planned merger between two banks that belong to two competing industrial groups, which has implications for economy-wide restructuring in Japan.

Lessons of the Japanese crisis

Kanaya and Woo conclude by drawing a number of lessons from Japan's banking crisis.

- In a financial system already characterized by overcapacity—like Japan's—deregulation can lead to excessive competition and risk taking. This problem is especially acute when unprofitable institutions are not subject to market forces.
- If deregulation is not coordinated and properly sequenced, it can be particularly harmful. "Regulatory arbitrage," for example, resulting from unequal regulatory and supervisory treatment of different financial institutions involved in similar activities, can lead to unhealthy competition and concentration of risk.
- Given the serious consequences for the financial system of property cycles and asset bubbles, banks must base lending decisions on cash-flow analyses of their borrowers and must reassess their creditworthiness in a timely manner.
- The Japanese main bank system relies excessively on the role of the main banks to monitor borrowers. If the main banks are themselves distressed, they may delay dealing with troubled borrowers, thereby worsening the problem.
- Weak corporate governance can prevent banks from restructuring to arrest their deterioration.
- Transparent accounting standards are important for effective supervision of financial institutions.
- Regulatory authorities must take a proactive approach toward supervision. If they exercise forbearance, they can postpone a crisis but will raise the fiscal cost of the final resolution. ■

Copies of IMF Working Paper 00/7, *The Japanese Banking Crisis of the 1990s: Sources and Lessons*, by Akihiro Kanaya and David Woo, are available for $7.00 each from IMF Publication Services. See page 94 for ordering information.

Available on the web (www.imf.org)

Press Releases

00/16: IMF Approves $83 Million Stand-By Credit for Lithuania, March 8

00/17: IMF Approves $7.2 Billion Three-Year Stand-By Credit for Argentina, March 10

00/18: IMF Receives Nomination for IMF Director, March 14

00/19: IMF Executive Director Withdraws Fischer's Nomination, March 16

News Briefs

00/12: IMF Executive Board Would Consider Augmenting Credit to Mozambique, March 3

00/13: IMF Completes Cape Verde Third Review Under the Stand-By Arrangement, March 6

00/14: IMF, World Bank, IDB, and CAF Prepared to Support Ecuador, March 9

Public Information Notices (PINs)

00/15: Hong Kong SAR, March 6

00/16: Belgium, March 3

00/17: United Kingdom, March 6

00/18: Guinea, March 8

00/19: South Africa, March 10

00/20: Nepal, March 14

Letters of Intent and Memorandums of Economic and Financial Policies

Argentina, March 15

Concluding Remarks for Article IV Consultations

Luxemburg, February 29 (preliminary)

Press Briefings

Transcript of a press briefing by Thomas Dawson, Director, IMF External Relations Department, February 29

Transcript of a press briefing by Thomas Dawson, Director, IMF External Relations Department, March 14

Other

Study Guide to *The Fabric of Reform*, an IMF video on economic change in Western Africa, February 29

Balance of Payments Coding System, March 6

IMF's Financial and Liquidity Position, March 14

Statement by Stanley Fischer, Acting IMF Managing Director, March 16

Statement by Executive Director Morais on Nomination Withdrawal, March 16

Notes: PINS are IMF Executive Board assessments of members' economic prospects and policies. They are issued following Article IV consultations—with the consent of the member—with background on the members' economies; and following policy discussions in the Executive Board at the decision of the Board.

Letters of Intent and Memorandums of Economic and Financial Policies are prepared by a member country and describe the policies that the country intends to implement in the context of its request for financial support from the IMF.

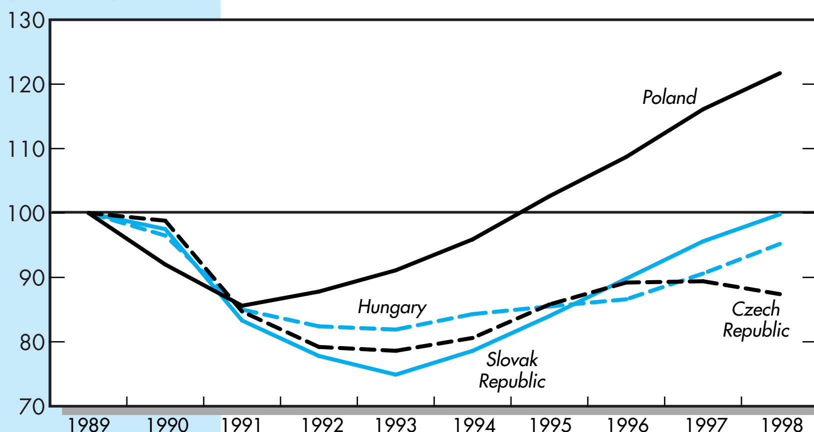
Concluding Remarks for Article IV Consultations. At the conclusion of annual Article IV discussions with the authorities, and prior to the preparation of the staff's report to the Executive Board, the IMF mission often provides the authorities with a statement of its preliminary findings.

IMF Working Paper

Rapid economic recovery earns Poland recognition as East European 'tiger'

When Poland began its transformation to a market economy in 1989, it was in a deep crisis and thought to be facing greater challenges than its central and eastern European neighbors. By late 1991, however, it had begun to recover and went on to register remarkably strong growth in the 1990s. In their IMF Working Paper *The "Soaring Eagle": Anatomy of the Polish Take-Off in the 1990s,* authors Mark De Broeck and Vincent Koen explain Poland's success, put its overall growth performance in perspective, and look at the country's growth prospects over the next few years.

Poland and neighboring countries: real GDP
(1989 = 100)



Data: National statistical offices

Although Poland's economic contraction was deeper than any the country had experienced since World War II, it was, according to De Broeck and Koen, shallower and shorter than in most of the other transition countries. From the onset of the recovery in 1991 through 1998, Poland enjoyed seven years of uninterrupted growth at an average rate of more than 5 percent a year, exceeding most official and unofficial projections. Poland outperformed its relatively successful central and eastern European neighbors (see chart, this page) and even more, the other transition countries.

Patterns of growth

De Broeck and Koen examined the available sectoral, ownership, and regional data to identify key features of Poland's growth and, despite the uneven quality of the data, were able to draw some broad conclusions.

During the 1990s, growth was driven first and foremost by industry, specifically manufacturing, while mining and agriculture stagnated (see chart, page 90). Although the centrally planned economies were widely perceived to be heavily oriented toward industry, the authors discovered less of a shift from industry to services in Poland than might have been expected. They attribute this paradox to the fact that services, broadly defined, encompass activities that were "overweight" under central planning (for example, freight and certain government administrative functions) alongside those that were underdeveloped (such as trade, hotels and restaurants, and financial intermediation). De Broeck and Koen point out that consumer-oriented services did, indeed, expand rapidly.

The 1990s witnessed a surge in the number of private sector firms and entrepreneurs. Between 1991 and 1998, the number of registered commercial law companies increased more than two and a half times, to 136,500; that of joint ventures rose almost eightfold, to about 37,000; and that of individual entrepreneurs increased more than 50 percent, to more than two million. This boom, the authors argue, reflects a correction to the distorted size distribution of industrial firms under central planning as well as the expansion of a small business sector. The authors point to another feature of Poland's performance in the 1990s—the greater dynamism in the private sector. The private sector share in output increased more rapidly than did its share in employment, particularly in industry. Productivity gains were thus higher in private than in public enterprises.

Turning to the regional dimension, growth appears not to have been uniform. De Broeck and Koen conclude that Warsaw and a few other large regions that recorded above-average growth were largely responsible for Poland's overall performance, with Warsaw alone accounting for about one-fifth of nationwide growth between 1992 and 1996. The main mining region (Katowice) also recorded above-average GDP growth despite the decline of the mining industry. The authors believe that in many regions the stagnation of certain sectors was offset by increased activity in other sectors, which, they suggest, might be indirect evidence that restructuring has been taking place.

Industrial output

In light of the important contribution of industry to Poland's growth performance, De Broeck and Koen further analyze the data for that sector to provide insight into the growth process. Between 1991 and 1998, the share of manufacturing in total industry rose to 90 percent, an increase of almost 12 percentage points, and output almost doubled. At a more disaggregated level, production increased in all manufacturing sectors but declined or even collapsed for a number of individual products. Production of radios and metal cutting machines, for example, dropped precipitously.

Over the same period, De Broeck and Koen report, the share of mining in total industry fell by half, to 5 percent. The contraction in this sector lasted through 1993, and output plummeted in 1998 against a background of weakening coal prices and rising imports.

Productivity and investment

Early in the recovery, improved resource utilization was the major determinant of growth in Poland. Before the beginning of Poland's transformation to a market economy and during the contraction, labor hoarding (defined as labor that would not have been employed if the economy had functioned as a market economy with the same level of output) occurred on a large scale. By the time output started to rally, there was a labor "overhang," or surplus, of about 30 percent. Employment gradually declined for two more years and expanded very little after 1993. By 1998, real GDP stood at 42 percent above its 1991 trough, but employment was not higher than it had been at the beginning of the decade. Labor productivity rose by about 6 percent a year during the initial phase of the recovery, but subsequently slowed down somewhat as the contribution of improved resource utilization to growth declined.

Labor productivity was boosted by an investment surge that helped quantitatively but also qualitatively rebuild a rather worn-out and obsolete capital stock. Investment boomed between 1994 and 1998, rising on average by 16 percent a year, with a strong foreign contribution. Poland's productivity gains, the authors say, largely reflect the country's response to the increasingly competitive environment facing its industries in the 1990s as trade surged—particularly manufacturing trade with the European Union (EU) countries—following the collapse of central planning and the consequent economic liberalization.

Ingredients of Poland's success

How was it possible for Poland to grow so rapidly given the monumental structural changes it faced during the transition to a market system? According to the authors, the country's success was due to a combination of relatively favorable initial conditions and fundamentally sound policies. The ingredients of the Polish success story include

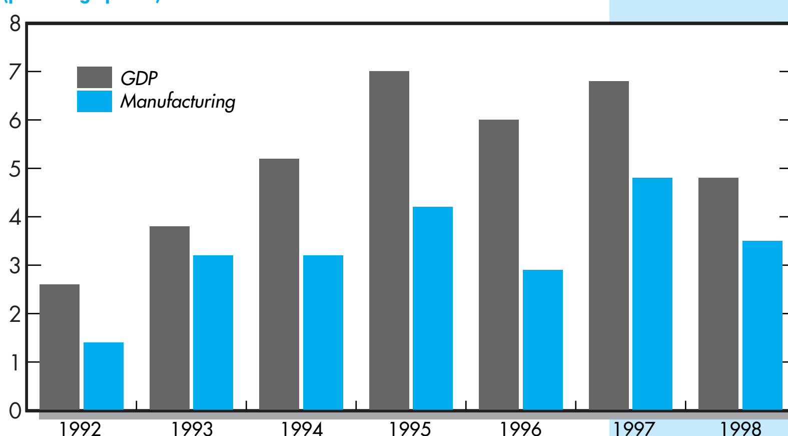
- an early political window of opportunity, as seen in a period of "extraordinary politics," during which the population showed a readiness to accept the costs of radical change;
- a sizable private sector at the start of the transition;
- early and comprehensive price and trade liberalization;
- early and broad dismantling of obstacles to foreign trade, which hastened the reorientation of trade toward the West and pressured firms to restructure;
- generous external debt relief, which paved the way for inflows of foreign direct investment;
- low entry barriers for new firms, which eased the way for labor to move from state-owned to new private enterprises;
- an established legal system that made contract enforcement possible;
- the imposition of hard budget constraints on public enterprises;
- entrepreneurial dynamism in the private sector;
- cautious macroeconomic policies, including an exchange rate policy designed to avoid overvaluation of the currency; and
- a relatively liberal social safety net that cushioned the social strains associated with restructuring.

Poland's prospects

In 1998 and early 1999, Poland's economy experienced a marked slowdown. The deceleration was partly due to temporary factors, namely, the tightening of financial policies (intended to restrain domestic demand and contain a widening current account deficit) and the adverse shock associated with the collapse in demand from transition countries farther east. But the slowdown also called into question the sustainability of rapid growth.

De Broeck and Koen anticipate that infrastructure weaknesses—including an inadequate road network and problems in the judiciary system—will hinder growth in the future. These shortcomings, they say, "slow down or altogether discourage certain business ventures but also facilitate corruption, which has been shown to be growth inhibiting." They also mention that the investment boom that helped Poland rebuild its capital stock may subside if corporate profitability, which began to deteriorate in 1998, continues to decline. In the plus column, the authors note that as unprofitable industries shrink, "the drag on overall growth from those sectors

Poland: contribution of manufacturing to overall GDP growth
(percentage points)



Data: Poland's Central Statistical Office and authors' calculations

will diminish." Sluggish growth would delay the needed adjustment in agriculture and heavy industry and would hamper the implementation of the ambitious structural reforms launched in 1999.

Although Poland grew more vigorously than other transition economies during the 1990s, a number of countries around the world recorded even faster growth during this period, and most countries experienced comparable episodes of robust growth in past decades. However, De Broeck and Koen stress, few of them faced challenges commensurate with those confronting the transition economies. Despite its recent growth record, Poland is unlikely to achieve the per capita income levels of the EU countries any time soon. Given the existing gap between Poland and the poorer EU members—Greece and Portugal—it might take Poland another generation to catch up even with these countries. ■

Copies of IMF Working Paper/00/06, *The "Soaring Eagle": Anatomy of the Polish Take-Off in the 1990s,* by Mark De Broeck and Vincent Koen, are available for $7.00 from IMF Publication Services. For details about ordering, please see page 94.

Extended Fund Facility Arrangements are designed to rectify balance of payments problems that stem from structural problems.

Stand-By, EFF, and PRGF Arrangements as of February 29

Member	Date of arrangement	Expiration date	Amount approved	Undrawn balance
			(million SDRs)	
Stand-By			**39,860.00**	**12,674.13**
Bosnia and Herzegovina	May 29, 1998	April 28, 2000	77.51	24.24
Brazil[1]	December 2, 1998	December 1, 2001	10,419.84	2,550.69
Cape Verde	February 20, 1998	March 15, 2000	2.50	2.50
Korea[1]	December 4, 1997	December 3, 2000	15,500.00	1,087.50
Latvia	December 10, 1999	April 9, 2001	33.00	33.00
Mexico	July 7, 1999	November 30, 2000	3,103.00	2,068.60
Philippines	April 1, 1998	March 31, 2000	1,020.79	475.13
Romania	August 5, 1999	March 31, 2000	400.00	347.00
Russia	July 28, 1999	December 27, 2000	3,300.00	2,828.57
Thailand	August 20, 1997	June 19, 2000	2,900.00	400.00
Turkey	December 22, 1999	December 21, 2002	2,892.00	2,670.28
Uruguay	March 29, 1999	March 28, 2000	70.00	70.00
Zimbabwe	August 2, 1999	October 1, 2000	141.36	116.62
EFF			**12,290.03**	**10,619.50**
Argentina	February 4, 1998	February 3, 2001	2,080.00	2,080.00
Azerbaijan	December 20, 1996	March 19, 2000	58.50	5.26
Bulgaria	September 25, 1998	September 24, 2001	627.62	313.82
Colombia	December 20, 1999	December 19, 2002	1,957.00	1,957.00
Croatia, Republic of	March 12, 1997	March 11, 2000	353.16	324.38
Indonesia	February 4, 2000	December 31, 2002	3,638.00	3,378.00
Jordan	April 15, 1999	April 14, 2002	127.88	106.56
Kazakhstan	December 13, 1999	December 12, 2002	329.10	329.10
Moldova	May 20, 1996	May 19, 2000	135.00	47.50
Pakistan	October 20, 1997	October 19, 2000	454.92	341.18
Panama	December 10, 1997	December 9, 2000	120.00	80.00
Peru	June 24, 1999	May 31, 2002	383.00	383.00
Ukraine	September 4, 1998	September 3, 2001	1,919.95	1,207.80
Yemen	October 29, 1997	March 1, 2001	105.90	65.90
PRGF			**3,494.51**	**1,943.65**
Albania	May 13, 1998	May 12, 2001	45.04	14.11
Azerbaijan	December 20, 1996	March 19, 2000	93.60	11.70
Benin	August 28, 1996	August 26, 2000	27.18	10.87
Bolivia	September 18, 1998	September 17, 2001	100.96	56.10
Burkina Faso	September 10, 1999	September 9, 2002	39.12	33.53
Cambodia	October 22, 1999	October 21, 2002	58.50	50.14
Cameroon	August 20, 1997	August 19, 2000	162.12	36.03
Central African Republic	July 20, 1998	July 19, 2001	49.44	32.96
Chad	January 7, 2000	January 7, 2003	36.40	31.20
Côte d'Ivoire	March 17, 1998	March 16, 2001	285.84	161.98
Djibouti	October 18, 1999	October 17, 2002	19.08	16.36
The Gambia	June 29, 1998	June 28, 2001	20.61	13.74
Ghana	May 3, 1999	May 2, 2002	155.00	110.70
Guinea	January 13, 1997	December 20, 2000	70.80	15.73
Guyana	July 15, 1998	July 14, 2001	53.76	35.84
Honduras	March 26, 1999	March 25, 2002	156.75	80.75
Kyrgyz Republic	June 26, 1998	June 25, 2001	73.38	38.23
Macedonia, FYR	April 11, 1997	April 10, 2000	54.56	27.28
Madagascar	November 27, 1996	July 27, 2000	81.36	40.68
Mali	August 6, 1999	August 5, 2002	46.65	39.90
Mauritania	July 21, 1999	July 20, 2002	42.49	36.42
Mongolia	July 30, 1997	July 29, 2000	33.39	15.95
Mozambique	June 28, 1999	June 27, 2002	58.80	50.40
Nicaragua	March 18, 1998	March 17, 2001	148.96	53.82
Pakistan	October 20, 1997	October 19, 2000	682.38	417.01
Rwanda	June 24, 1998	June 23, 2001	71.40	38.08
Senegal	April 20, 1998	April 19, 2001	107.01	57.07
Tajikistan	June 24, 1998	June 23, 2001	100.30	40.02
Uganda	November 10, 1997	November 9, 2000	100.43	17.85
Yemen	October 29, 1997	October 28, 2000	264.75	114.75
Zambia	March 25, 1999	March 24, 2002	254.45	244.45
Total			**55,644.54**	**25,237.28**

[1]Includes amounts under Supplemental Reserve Facility.
EFF = Extended Fund Facility.
Figures may not add to totals owing to rounding.
PRGF = Poverty Reduction and Growth Facility.
Data: IMF Treasurer's Department

IMF approves $7.2 billion three-year Stand-By credit for Argentina

On March 10, the IMF announced that it had approved a three-year Stand-By credit for Argentina. The new Stand-By credit replaces the Extended Fund Facility approved on February 4, 1998 (see Press Release 98/01, *IMF Survey*, February 9, 1998, page 43). The credit, in an amount equivalent to SDR 5.4 billion (about $7.2 billion), will be used to support the government's 2000–02 economic program. The Argentine authorities have indicated that they intend to treat the credit as precautionary.

Commenting on the Executive Board discussion on Argentina, Acting IMF Managing Director Stanley Fischer commended the Argentine government, saying that it has "embarked on a strong economic program aimed at promoting the recovery and sustained growth of the economy, with continued price stability, and an external current account maintained within financeable limits." Excerpts from his statement follow.

"The program contains a significant fiscal consolidation, which will permit a gradual increase in national savings to finance the recovery of investment and reduce the external debt burden over time. The macroeconomic adjustment is underpinned by comprehensive structural reforms.

"The strengthening of the public finances involves expenditure restraint, a significant additional tax effort, and measures to strengthen tax administration. The authorities have moved decisively in these areas, and most of the envisaged measures under the program are already in place.

"The structural reform agenda is comprehensive and far-reaching. The reforms in the fiscal area, including the proposals to strengthen the social security system and to modify the revenue-sharing regime with the provinces, will be essential to secure a lasting improvement in the public finances, as well as to improve the equity and efficiency of both taxation and public spending. The proposed labor market reform and deregulation should help create the conditions for improvements in productivity and increases in employment. Implementation of these structural measures is critical, both to contribute to the sustainability of the fiscal adjustment and to strengthen competitiveness and economic growth," Fischer said.

Program summary

The adjustment and reform program that the IMF credit will support is based on a rate of GDP growth of 3½ percent in 2000, which would accelerate to 4 percent in subsequent years as firm implementation of the appropriate policies strengthens confidence and improved competitiveness facilitates further growth of exports.

To these ends, the program targets a 3½ percent of GDP reduction in the consolidated public deficit over the period 2000–02, about half of which is to take place in 2000. The primary balance of the public sector will shift to a surplus of 3¾ percent of GDP in 2002 from a small deficit in 1999. The authorities expect to achieve these results by eliminating distortions in the tax system; further broadening the tax base; strengthening tax enforcement and compliance; increasing transparency and cost effectiveness in the use of public resources; and reforming fiscal relations between the national and subnational levels of government with a view to increasing fiscal responsibility, transparency, and equity.

Besides initiatives aimed at promoting a lasting improvement in the public sector finances, the wide-ranging program of structural reforms includes that of labor market legislation. Additional reforms are also planned in the social security system to ensure its long-term solvency and to make it more equitable, and in the promotion of competition in sectors that enjoy quasi-monopoly positions or are in need of modernization, such as those in the telecommunications and energy sectors.

The authorities plan to improve and expand social assistance programs within the limits of the budget by identifying and eliminating problems of duplication, deficient targeting, and high administrative costs.

Argentina joined the IMF on September 20, 1956. Its quota is SDR 2.1 billion (about $2.9 billion). Its outstanding use of IMF credit currently totals SDR 3.1 billion (about $4.2 billion). ■

The full text of Press Release No. 00/17 is available on the IMF's website (www.imf.org).

Members' use of IMF credit
(million SDRs)

	During February 2000	January–February 2000	January–February 1999
General Resources Account	**260.00**	**261.42**	**508.02**
Stand-By Arrangements	0.00	1.42	0.97
EFF	260.00	260.00	98.03
CCFF	0.00	0.00	409.02
PRGF[1]	**29.30**	**50.01**	**157.85**
Total	**289.30**	**311.43**	**665.87**

EFF = Extended Fund Facility
CCFF = Compensatory and Contingency Financing Facility
PRGF = Poverty Reduction and Growth Facility

Figures may not add to totals shown owing to rounding.
[1]Formerly ESAF—the Enhanced Structural Adjustment Facility.

IMF, World Bank, IDB, and CAF to propose $2 billion support package for Ecuador

In a news brief issued on March 9, the managements of the IMF, the World Bank Group, the Inter-American Development Bank (IDB), and the Corporación Andina de Fomento (CAF) announced their intention to propose to their Executive Boards a support package for Ecuador. The text of News Brief No. 00/14 is available on the IMF's website (www.imf.org).

The proposed package, amounting to $2 billion, would be made available over the next three years to support the government of Ecuador's ambitious program of economic and structural reform. The package comprises a Stand-By Arrangement of $300 million from the IMF that is expected to be presented to the IMF's Executive Board within a month and would be disbursed during the next 12 months. In addition, the proposed package consists of new loans totaling $425 million from the World Bank Group, $620 million from the IDB, and $700 million from CAF.

If approved by the Executive Boards of the institutions, $900 million will be available to Ecuador in the next 12 months.

The loans are a combination of balance of payments support and investment lending with a strong social content. They are intended to assist the implementation of dollarization and the resolution of the banking crisis, and to strengthen the public finances, including Ecuador's social safety net, to minimize the impact on the poor of the nation's difficult economic situation.

Disbursements this year are likely to begin within a month, by which time the Ecuadoran Congress is expected to have approved complementary measures necessary to implement Ecuador's reform program. ■

Recent publications

Books

Post-Bubble Blues: How Japan Responded to Asset Price Collapse, Tamim Bayoumi and Charles Collyns ($26.00)

Working Papers ($7.00)

00/24: *A Framework for Price Statistics*, Kimberly D. Zieschang

00/25: *Financial Crisis and Credit Crunch in Korea: Evidence from Firm-Level Data*, Eduardo Borensztein and Jong-Wha Lee

00/26: *Shadow Economies Around the World: Size, Causes, and Consequences*, Friedric Schneider and Dominik Enste

00/27: *Estimation of Trade Protection in Middle East and North African Countries*, Maria-Angels Oliva

00/28: *Devaluation Expectations and the Stock Market: The Case of Mexico in 1994/95*, Torbjörn Becker, R. Gaston Gelos, and Anthony J. Richards

00/29: *The Choice of Exchange Rate Regime and Monetary Target in Highly Dollarized Economies*, Andrew Berg and Eduardo Borensztein

00/30: *The Transition Economies After Ten Years*, Stanley Fischer and Ratna Sahay

00/31: *Trade Policy in Financial Services*, Natalia Temirisa, Piritta Sorsa, Geoffrey Bannister, Bradley McDonald, and Jaroslaw Wieczorek

00/32: *The Great Contractions in Russia, the Baltics, and the Other Countries of the Former Soviet Union: A View from the Supply Side*, Mark De Broeck and Vincent Koen

00/33: *Two Approaches to Resolving Nonperforming Assets During Financial Crises*, David Woo

IMF Staff Country Reports ($15.00)

00/18: Dominica: Statistical Annex

00/19: Jamaica: Selected Issues and Statistical Appendix

00/20: Thailand: Statistical Appendix

00/21: Thailand: Selected Issues

00/22: Croatia: Selected Issues and Statistical Appendix

00/23: Switzerland: Staff Report for the 2000 Article IV Consultation

00/24: Australia: Selected Issues and Statistical Appendix

00/28: Republic of Croatia: Staff Report for the 1999 Article IV Consultation

00/30: People's Republic of China—Hong Kong SAR: Staff Report for the 1999 Article IV Consultation

00/31: Belgium: 1999 Article IV Consultation

00/32: United Kingdom: Staff Report for the 1999 Article IV Consultation

Other publications (free)

The Per Jacobsson Lecture: The Past and Future of European Integration—A Central Banker's View by European Central Bank President Dr. Willem F. Duisenberg

The IMF and Human Development: A Dialogue with Civil Society, Michel Camdessus

Publications are available from IMF Publication Services, Box X2000, IMF, Washington, DC 20431 U.S.A. Telephone: (202) 623-7430; fax: (202) 623-7201; e-mail: publications@imf.org.

For information on the IMF on the Internet—including the full texts of the English edition of the *IMF Survey*, the *IMF Survey*'s annual *Supplement on the IMF*, *Finance & Development*, an updated *IMF Publications Catalog*, and daily SDR exchange rates of 45 currencies—please visit the IMF's website (www.imf.org). The full texts of all Working Papers and Policy Discussion Papers are also available on the IMF's website.

IMFSURVEY

Rise in social spending under IMF programs continues, but benefits are unequal

A recent review of data on government spending on education and health care reveals that such spending has continued to grow in countries with IMF-supported programs (see *IMF Survey*, March 8, 1999, page 79; February 23, 1998, page 52; and July 21, 1997, page 217). Indicators of education attainment and health status have also continued to improve. But underlying the increase in average spending are significant differences among countries and an uneven distribution of the benefits. The review, which covers 66 countries with IMF-supported programs during 1985–98, is part of an ongoing effort by the IMF to compile and analyze data on government spending in the education and health care sectors.

Average trends

Under IMF-supported programs, public spending on both education and health care has increased on average, both as a share of GDP and total spending and in real per capita terms, and social indicators have improved (see top chart, this page). Average spending growth slowed during 1998, but was not out of line with developments in earlier years. The spending increases were, on average, equally split between current and capital outlays.

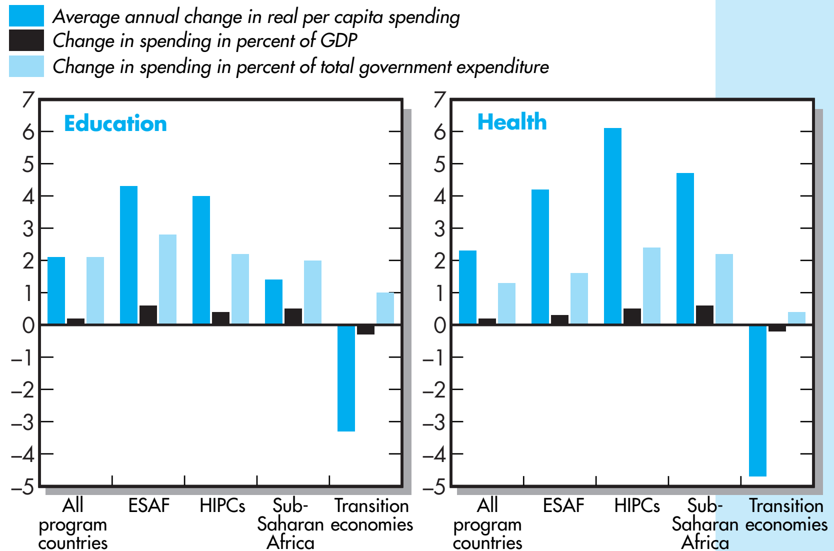
Variation in spending across countries

The averages mask substantial variation across countries and within regions. Public education and health care spending have increased in real per capita terms in just under two-thirds of the countries with IMF-supported programs. On average, the largest spending decreases in real per capita terms have taken place in countries where such spending was relatively high and inefficient at the outset of the program (most notably in transition economies).

The variation in spending trends has been especially large in sub-Saharan Africa. This region includes four of the countries with the largest declines in real per capita education spending under IMF-supported programs (the Republic of Congo, Côte

Social spending in countries with IMF-supported programs[1]

(average change)[2]

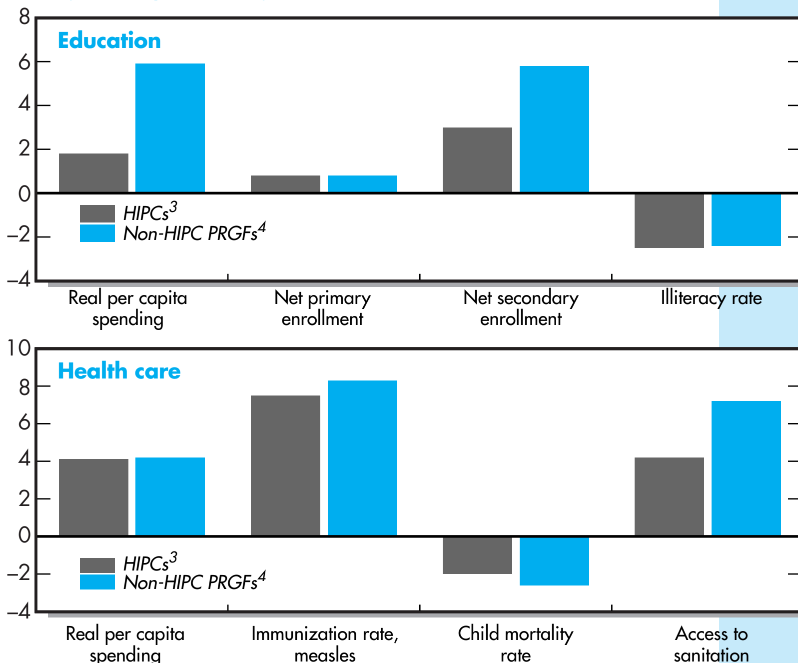


[1]Reflects all countries with IMF-supported programs for which data are available.
[2]Between preprogram year and most recent year for which data are available.

Data: National authorities and IMF staff estimates

Change in social spending and social indicators in HIPCs and in PRGF-eligible countries[1]

(average annual percent change)[2]



[1]Reflects countries for which data are available.
[2]From first year since 1985 for which data are available to most recent year for which data are available.
[3]Heavily indebted poor countries eligible for debt relief under HIPC Initiative.
[4]Non-HIPC countries eligible for the Poverty Reduction and Growth Facility. Excludes transition economies: Albania, Armenia, Azerbaijan, Bosnia and Herzegovina, Georgia, the Kyrgyz Republic, former Yugoslav Republic of Macedonia, Moldova, Mongolia, and Tajikistan.

Data: World Bank, World Development Indicators database; national authorities; and IMF staff estimates

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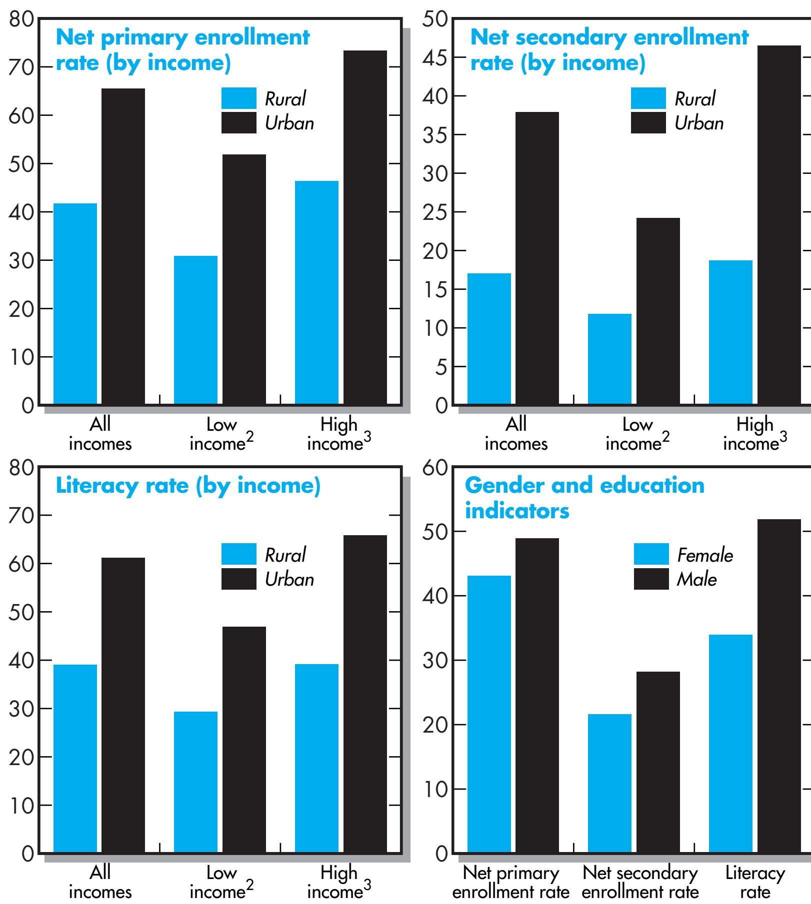
d'Ivoire, Madagascar, and Niger), as well as four of the countries with the largest increases in such spending (Burkina Faso, Cameroon, Ethiopia, and Lesotho). Both the level and the growth in spending on social sectors have been relatively low in highly indebted poor countries (HIPCs)—that is, countries that are eligible for relief of external debt under the HIPC Initiative—compared with other countries that are eligible for the IMF's new Poverty Reduction and Growth Facility (PRGF) (see bottom chart, page 95). At the same time, the improvement in social indicators has been slower in HIPCs than in other PRGF-eligible countries.

Distribution of social indicators within IMF program countries, 1992–97[1]

(percent)



[1]Reflects countries for which data are available.
[2]Households in the bottom 20 percent of the income distribution.
[3]Households in the top 20 percent of the income distribution.

Data: World Bank, African Development Indicators 1998/99; and World Bank, *Poverty Assessment Reports* (various issues)

Benefits of social sector spending

The distribution of benefits of spending on education has been uneven within countries, as reflected in lower levels of indicators of education attainment in rural areas, for women, and in low-income households (see chart, this page). Preliminary data from household surveys in various countries show similar inequities for indicators of health care received (for example, infant mortality, immunization, births attended by skilled personnel, and access to sanitation). The uneven distribution of benefits from public spending on social sectors is exacerbated by the high share of resources devoted to nonbasic services available primarily to higher-income households (for example, 58 percent of total public health care spending is allocated to curative health care, and 19 percent of education spending, to tertiary education).

These results have two important implications for the preparation of poverty reduction strategy papers (these are country-driven documents identifying priority public action for poverty reduction; see *IMF Survey*, January 10, page 3). First, increased outlays on antipoverty programs in the context of debt relief for HIPCs should not perpetuate existing inefficiencies in public spending on education and health care. Second, careful attention needs to be paid to the targeting of public services to rural areas, women, and low-income households. ■

Sanjeev Gupta, Robert Gillingham,
Marijn Verhoeven, and Erwin Tiongson,
IMF Fiscal Affairs Department

Selected IMF rates

Week beginning	SDR interest rate	Rate of remuneration	Rate of charge
March 6	4.16	4.16	4.73
March 13	4.20	4.20	4.78

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 (as of May 1, 1999, the U.S. dollar was weighted 41.3 percent; euro (Germany), 19 percent; euro (France), 10.3 percent; Japanese yen, 17 percent; and U.K. pound, 12.4 percent). The rate of remuneration is the rate of return on members' remunerated reserve tranche positions. The rate of charge, a proportion (currently 113.7 percent) 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/external/np/tre/sdr/sdr.htm).

Data: IMF Treasurer's Department