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VIDEO CONFERENCE OF MR. BOORMAN WITH ASIAN JOURNALISTS ON THE IMF'S REVIEW OF IMF-SUPPORTED PROGRAMS IN INDONESIA, KOREA, AND THAILAND

January 19, 1999
7:30 a.m.
IMF Headquarters
Washington, D.C.

MR. ANJARIA: I'd like to thank first of all Mr. Thomas Chan of the Hong Kong Monetary Authority for making the arrangements and facilitating this event at the Hong Kong end, and also Mr. Donal Donovan, the director of the IMF Singapore Training Institute, for doing the same at the Singapore end. Above all, I'd like to thank the journalists who are present, especially those who have come from some distance away and given the fact that today happens to be a public holiday in Singapore and Jakarta.

As you know, we are releasing today this new study called "IMF-Supported Programs in Indonesia, Korea and Thailand: A Preliminary Assessment." This study is an important one and has been authored by staff in the Policy Development and Review Department of the IMF.

Mr. Boorman, who heads that department, has been with the Fund for a number of years and he's not a stranger to Asia. He spent four years in Jakarta many years ago working in the field, familiarizing himself with Indonesia and other countries.

This, to us, is a special event, not because we are publishing a review of IMF programs and operations, because you only have to look at the publications catalogue of the IMF to see that a number of these reviews have been published from time to time. It is a special event because we are looking for the first time at the Asian crisis countries and because we have the opportunity and good fortune to discuss and to answer questions with journalists from the region itself.

The paper was discussed by the Executive Board of the IMF on December 21 and I'm especially pleased that we're able to make it available to the public through you just a few working days after that event.

Now just by way of preliminaries I should mention that the report and the contents of this briefing are under embargo. It is just after 8:30 p.m. in Hong Kong and Singapore and the embargo is for 2 a.m., 02:00 hours on January 20. At that time we would also post the report on the external website of the IMF, which is at www.imf.org.

I would like to conclude my comments now and ask Mr. Jack Boorman to make some introductory remarks, after which we will move to your questions and answers.

MR. BOORMAN: Thank you very much, Shail, and good evening, ladies and gentlemen. Thank you for coming to participate in this session. Thank you, Mr. Chan, for organizing in Hong Kong and Donal Donovan in Singapore. It's good to see you, even if from this distance.

Ladies and gentlemen, you have before you this document, the first part of which, the white pages, is a staff paper on the crisis in Korea, Thailand and Indonesia; and in the back of that document the blue pages reproduce the Chairman's summing up of the Executive Board meeting that was held to discuss the staff report.

Before taking your questions I'd like to say a little about each of these documents. The staff paper, which was prepared under the direction of Mr. Tim Lane, who is here with me, is the first systematic internal review of the IMF's approach to helping the three countries that were most severely affected by the Asia crisis.

It looks at the causes of the crisis, it looks at the Fund's response in terms of both policy advice and financial support for these countries, and it tries to assess the early experience of the countries involved.

In essence, the paper says that the policies the Fund recommended, and which to varying degrees Indonesia, Korea and Thailand have followed, were broadly appropriate in the circumstances and given what was known at the time the programs were formulated and as they have been revised.

Most importantly, a few basic conclusions. One, that higher interest rates were needed at the outset of these programs to prevent the currencies from going into a worse downward spiral than in fact occurred.

Secondly, that tighter budgets appeared to be justified at the outset based on the Fund's--and I would say also others'--initial assessment of the prospective depth of the recession. But it also says that a loosening in those fiscal policies was seen to be needed as the depth of the crisis unfolded. There is here surely a question as to whether the loosening of policy might possibly have been implemented somewhat sooner.

Thirdly, the paper says that the emphasis on structural policies--financial sector reform, corporate restructuring and the other elements that were key to the programs adopted by these countries--was appropriate. I'll come back to that point in a moment.

Let me say as an aside that this paper, the staff's paper, is part of the IMF's established practice of internally reviewing its own work. This is one of the main functions of the department which I head, the Policy Development and Review Department, as Mr. Anjaria has mentioned, and it explains why it's me rather than, for example, Mr. Neiss, who's head of the Asia Department, who's sitting here talking to you today.

I might also mention that recent reviews of other aspects of the IMF's work, such as its programs under the concessional facility, the so-called ESAF, have been prepared recently and have also been published, as this one is going to be.

There is also a process in the Fund of external evaluation. External evaluation of ESAF was also conducted and there is a published version of that report available from the Fund. Similarly, an external evaluation of the way in which the Fund conducts its surveillance is currently under way and I expect something will come out of that exercise and be published perhaps next summer.

Back to the crisis, if I may. The outlines of the crisis are familiar to all of you. You've been covering it in depth and we've been following what you've been saying.

Let me say in passing that this paper looks at the experience with IMF-supported programs as they evolved up to about October of 1998. More recent developments are covered in other documents--the World Economic Outlook, which came out in December, and the International Capital Markets Report, also released in December.

This crisis differed from those that typically involve the IMF most importantly because it did not arise from profligate government spending and monetary financing of that spending, as is the case in so many other countries which the Fund supports with its assistance.

It occurred in a world where volatile financial markets can move with devastating speed. If emerging problems, as were evident in Thailand, for example, are not dealt with in a timely manner, the room for maneuver that remains open to the authorities shrinks dramatically.

Once that initial period for timely action has passed, the challenge for the countries concerned and indeed for the IMF and the international community in supporting them has to be to find policies that quickly can halt a crisis and then promote lasting economic growth.

Stemming a crisis of confidence that's manifested in the collapse in the value of a currency and that brings with it a risk of hyperinflation leaves a government little choice but taking tough monetary policy actions. All three countries increased interest rates somewhat to make holding the domestic currency more attractive but in the view of the report, they did not act soon enough or boldly enough to head off a full-blown crisis.

All the countries are now, however, seeing the benefit of tightened monetary policy, as the restoration of currency stability allows interest rates to decline. In Korea and Thailand, as you've seen, those interest rates have now declined to precrisis levels.

I put this very briefly but the paper itself, reflecting the intense interest in this particular aspect of these programs, tackles the subject at considerable length. The report concludes in essence that if we were making these decisions again we would, if anything, call for prompter and more aggressive action along similar lines.

Fiscal policy is another important topic covered in the paper. Here a degree of budget-tightening was envisaged at the outset of each of the three programs, in part to pay for some of the substantial and inevitable costs of reform of the financial sector. This tightening was planned at a time when the Fund, like most other observers, thought these countries could get away with a comparatively mild slowdown in growth.

The tightening was put into reverse once it became apparent that the recessions these countries faced were going to be deeper than expected and that expansive budget policies would be needed to help cushion the economies as the recessions developed.

The message here I think is twofold. First, there was good reason from the standpoint of halting the slide in confidence for guarding against fiscal slippage initially. And the extent of the actual tightening of budgets should not be overstated.

But the budget targets established in the programs were predicated on a view of macroeconomic prospects that turned out, in hindsight, to be mistaken and the easing of policy could have come more promptly as circumstances changed.

Mentioning that the recession has been deeper than anticipated brings me to another important part of the paper--its discussion of why original projections were overly optimistic.

The message of the paper here is a bit tricky and nuanced. Yes, there were optimistic projections but these projections were predicated on the programs working as planned. And this, in turn, depended on forceful implementation and a quick return of investor confidence.

That these projections did not materialize is the result of several factors that are enumerated in the paper, including a lack of clarity in certain policies, hesitancy on the part of governments in carrying out their own policies and, of course importantly, the reaction of financial markets.

As you'll see, the paper gives a lot of attention to structural policies, making the point that a major focus was needed in this area to address the root causes of the problem--notably the vulnerabilities in the financial and the corporate sectors.

It's in the nature of structural policies that they take time to yield results and it is, in my view, premature to conclude that these have been overambitious or too diffuse. Certainly there can be questions in hindsight about some of the specific measures taken, as well as the pace and sequencing of these measures. It would be odd indeed if there were not, given the ambitiousness of these programs.

But in reviewing the programs we remain convinced that comprehensive financial and corporate structural reforms were needed at the very center of the programs in these three countries.

Finally on the staff report itself, there's a discussion of social safety nets that were strengthened and indeed in some cases created anew to alleviate the human cost of the crisis. The paper highlights the collaboration that's taken place between the IMF, the World Bank and the Asian Development Bank in this important area.

Lastly a few words about the blue pages in this manual, the summing up. For those of you that aren't familiar with the jargon of the IMF, a summing up is a statement made by the chairman of the Executive Board, in this case the Managing Director, at the end of a board discussion of certain topics.

The summing up is an attempt to pull together the views expressed by Executive Directors who are the 24 officials who represent the 182 member countries of the IMF. This summing up is rather long and inevitably so because it tries to capture what was a long and deep discussion about this paper.

On the main themes, the board agreed with the staff's view of the exceptional nature of this crisis and the comprehensive focus of programs, embracing both macroeconomic and structural policies, as well as unprecedentedly large external financing.

They agreed that in the midst of the crisis, the formulation of programs on the basis of floating exchange rates was the only sensible approach that was available and noted that the main goal of monetary policies in these countries was to avert a depreciation-inflation spiral and that in this, the programs, after a hesitant start, had been successful.

This inflation or depreciation-inflation spiral is a real risk which I believe is underplayed in the discussions of the crisis that have taken place outside the IMF.

The directors also noted that initially there had been a need for fiscal adjustment to prevent an expansion of fiscal deficits. Those directors saw a central lesson of the importance of on-going efforts to involve the private sector in forestalling and resolving financial crises.

Nevertheless, and this is not unusual in the context of an operation as complex as this, there were a range of views in the Board on some aspects of the programs. These are fully covered in the summing up.

I might say that to get a feel for what I might call the center of gravity of the views in the board, you have to take seriously the introductory phrases characterizing the views of directors, these phrases such as "a few," "several," "many," "others." Donal Donovan perhaps can explain that to the people in Singapore. This is an art of the Secretary of the Board. But they do need to be taken seriously to capture where the center of the Board is on a particular issue.

The purpose of this exercise has been to draw on the experience that we and the countries have had to date and to look hard and honestly at the crisis and to provide observers outside the Fund with our own analysis and our views in a concise manner.

While the jury is still out on a number of subsidiary questions, there are lessons emerging from the greater clarity of hindsight. Certainly there are things that can be done in advance to forestall crises, such as increasing the transparency of financial information and improving financial supervision and regulation in all countries.

We're also examining, as you know, ways of promoting greater private sector involvement in forestalling and, when they occur, in resolving financial crises. We're also looking at issues regarding the adequacy of official financing.

A number of these lessons are already being explored in the context of the discussions which are going on here in the IMF but also in an array of fora around the world on the international financial architecture. These discussions will continue. We will, as you know, be reporting on these discussions as well in the context of the meetings of the interim committee that will take place towards the end of April. Thank you very much.

MR. SHASTRY: We'll now move on to questions. We'll alternate between Singapore and Hong Kong. We request the journalists identify themselves before asking the question.

MR. KHANNA: Good morning, all in Washington. It's nice to see you all. Some of you I've seen before.

I've had the opportunity to read the report, albeit I read it hurriedly, and I have a couple of questions but I'll just ask one for now.

The Fund seems to have admitted that, in fact, it contributed to the bank runs that occurred in Indonesia after the closure of 16 banks in November of 1997.

What lots of people seem to feel is that was the point at which things in Indonesia went crazy, so to speak. When the rupiah was approximately 4,000 to 5,000 to the U.S. dollar around the end of November but it was in early December that it kind of took off vertically and went to 12,000 within a matter of weeks.

I just wonder if you could tell us how central was that episode in creating the breakdown of both the program, as well as the economic dislocation that followed in Indonesia?

MR. BOORMAN: This is one of the most difficult questions I think to wrestle with in the context of this entire exercise. This is one of the most difficult aspects of this experience that we have had and one of the most difficult questions to address. Let me take it in two parts.

On the point that you make about the exchange rate, I'd suggest and encourage you to conduct a little exercise that we did. Chart the pattern of the Indonesian rupiah from the beginning of the crisis to let's say the middle of 1998 and you'll see major episodes of weakening. Time those to various things that were happening, such as, for example, the closure of the 16 banks but also to various other events that were occurring at the same time--the rumors of President

Suharto's illness, the announcement of Mr. Habibie as the candidate for vice president, and so forth.

Those political and economic events show up extraordinarily interestingly in the pattern of the development of the rupiah. And one of the things I think that comes out of that is that the connection of that decline to the closure of the 16 banks is relatively modest in the context of the overall decline in the rupiah that took place.

Secondly, on the closures themselves, this is an issue that all of those of us who were involved in that decision agonized about greatly. One of the early lessons that were learned in the course of this crisis was that guarantees or perceived guarantees had lain behind what I might say was at best casual if not irresponsible behavior on the part of certain creditors and debtors.

In Thailand, for example, the fixity of the exchange rate over such a long period of time, which had served the Thai authorities and policymakers very well, also created a sense that you were not at risk in accepting foreign exposure in Thailand.

Similarly, guarantees that had been issued in Korea in August over the liabilities of the banking system had an influence on the way people behaved.

In the light of that experience there was a hesitancy to expand blanket guarantees validating bad decisions, if you want, by creditors, in the context of a situation of the banking crisis in Indonesia. That's one of the reasons why only a limited guarantee was offered on bank deposits.

I think there were problems in the way in which that guarantee was promulgated and explained. It is my impression, though you people sitting in Jakarta would know better, that the existence of the guarantee was not terribly well publicized, it was not clear the extent to which people had confidence in it, and we know that people who even would have been covered by the guarantee were withdrawing their deposits from the banks.

But this goes perhaps to the fundamental issue of the closure, and that is why close those banks at that time? And the answer to that from our point of view is it was no secret that there were weaknesses and severe weaknesses in the Indonesian banking system. It was no secret that Bank Indonesia was working with a number of troubled banks and had various lists categorizing banks in different classifications of weakness. It was no secret the incredibly weak state of a number of the private banks, the number of which had exploded in the early 1990s. And it was the feeling--on both sides--in discussing with the Indonesian authorities, that a signal had to be given that the authorities were going to come to grips with this problem by dealing, as they have to deal, with weak banks in the system and to close them.

The question that has been on our mind is not so much whether or not those banks should have been closed but first, whether or not the guarantee issue was properly dealt with; and secondly, some of us believe there's a serious question as to whether or not a sufficient number of banks were, in fact, closed.

MR. SALUDO (Asia Week): Good morning. Looking at the report and also at the conclusions, I don't seem to detect a large amount of it being devoted to the social and human costs of the crisis.

Is there some review, as well, of this aspect of the crisis and perhaps some kind of guidelines as to how much pain, so to speak, is acceptable in devising programs for future crises? Is this now part of the thinking in the Fund? You know, how much unemployment is acceptable? In Indonesia tens of millions were pulled below the poverty line. How much of that is acceptable?

MR. BOORMAN: That's a good question. I think we need to take the issues that arise from this crisis in several bites. And the intent of this part of the exercise was essentially to look at the broad design of the programs--their macroeconomic aspects and the structural aspects in particular.

We do and we have looked at the social content of these programs but you're right to point out that it's not in the depth that we have covered the issues about fiscal policy, the stance of monetary policy, the issue of floating the exchange rates and so forth.

The reason for this is we wanted to get a grasp of the issues that had arisen regarding the broad macroeconomic and structural thrusts of these programs. We wanted to take seriously the criticisms and comments that have been made by observers outside regarding the stance, for example, of fiscal policy, regarding the use of interest rates in the context of a depreciating exchange rate and these other very important issues that have been put on the table.

This is not by any means to minimize the importance of the social aspects, but as you know, in each one of these programs we are not by ourselves, the Fund alone, working on these social issues. In Korea, for example, the implementation of an unemployment compensation scheme is very much an activity of the World Bank and it is one of the key areas of social action in the Korean program.

Similarly, the public works projects, if I can use that phrase, in Thailand to create employment in certain areas is also being directed by the World Bank. We're cooperating with the Bank and working with them on rice distribution and rice issues generally in Indonesia and so forth.

We will at some point have to go more deeply into these questions. We have been as busy as we can be in trying to move with an evolving situation to cover the social aspects of these programs, very much in the context of work with the other two institutions who are deeply involved, and we will need to stand back and review in more depth those aspects of these programs.

QUESTION: The IMF explains that the policy is not as effective as expected because of the severity of the situation and you said in a similar situation of course again you would take prompter and more aggressive policies.

Isn't there an alternative, including relying more on people from the region for input?

MR. BOORMAN: On the issue of whether we would advise prompter, more aggressive policies in the context of a similar crisis, I think we need to make a distinction.

The conclusion I was trying to draw on that front regarded monetary policy and the use of interest rates. And I think what we see, notwithstanding the criticism that has been lodged at the Fund for that aspect of policy in these cases, we do see that beginning in January when Korea and Thailand in particular aggressively moved interest rates to protect the currency and signaled to the market that they were going to hold to those interest rates until the currencies appreciated, that this has substantially worked.

Those currencies first stabilized. They have now appreciated substantially and in the wake of that appreciation interest rates have been able to come back down rather dramatically.

The conclusion that we tend to draw from that experience is that that stabilization and reversal of the currency depreciation could have occurred earlier and perhaps with less pain if interest rates had been used more aggressively earlier in the game. So we have no apologies for the advice on monetary policy that we have provided there.

On the fiscal side, that's a tough call. The paper is at pains to describe the kind of fiscal adjustment that was recommended in the beginning and then the adjustment to that policy which took place as the programs unfolded.

It's a tough call because you have to make certain assumptions about whether the program is or is not going to work. To the extent that it's going to work, you end up with macro projections that then generate a certain fiscal profile.

I think what's important on that front is to do what we did and that is remain flexible. And in the case of--take your country, Indonesia, for example--in the program which has just been discussed with the authorities going forward, there is a deficit on the order of 6 percent of GDP incorporated into the program to provide support to economic activity.

On the other issue you raise, regional inputs and the thought that people in the region understand these economies better than perhaps people outside the region, I think it is critical to have a regional input and it's particularly critical to have what we in the Fund have come to call ownership of the programs.

You cannot force a policy package on country authorities from Washington, from anyplace else, and expect the country to forthrightly implement the kind of policies that are needed to address a situation like this.

The authorities have got to buy into those policies. They have got to believe that they are absolutely the right policies. And we work hard to try to make sure that the authorities are indeed owning the policies that are recommended in the context of our programs.

MR. BOWRING (*International Herald Tribune*): I don't think we begrudge the Fund the opportunity to defend itself as far as possible and I won't go into any of the details in this interesting document. My questions relate to what isn't in this document.

In the first place I don't see any significant discussion at all about the reasons for the huge flow of short-term capital into the region in the 18 months prior to mid-1997 or an explanation as to why there was this huge and sudden exodus, change of heart among international bankers.

No examination at all, as far as I can see, of the role of banks in other member countries, particularly in Europe and Japan, in precipitating both the in-flow and the out-flow.

No mention at all of the supervisory responsibilities of central banks in those countries as far as capital flows are concerned; no mention at all of how much of IMF funds and indeed of the guarantees which governments, particularly in Korea, were required to give to private sector foreign banks, how much that cost those governments and why those banks should have been rescued in this way.

No mention at all of the question of moral hazard as far as foreign banks are concerned. There's a huge gap, it seems to me, in your approach to the whole question of the reasons for the crisis in Asia.

My second question relates to another rather less significant gap but that is the cumulative impact of your various policies, not only in the countries which you dealt with directly--i.e., Korea, Thailand and Indonesia--but in the knock-on impact that those policies had in other countries. I would mention specifically Malaysia in that context, which was certainly advised to follow IMF programs. And, in fact, if you look at the data you find that, in fact, Malaysia is perceivably actually worse off than at least Thailand at the present time.

Did you consider at all the cumulative impact of your national policies pursued in the particular countries under consideration?

MR. BOORMAN: A couple of comments on your question. First, you start by saying it's right for the IMF to defend itself. This was not started, nor was it carried out, as a defense. It was carried out as an assessment and an evaluation of the experience that we had had in the context of these programs.

On the other issues you raised about essentially the comprehensiveness of the paper, these other issues that we should have gone into, I'd point again, as I did in my opening remarks to the work that's done in the context of our International Capital Markets Reports, the last version of which was put out in December. The comprehensive annual issue of the International Capital Markets Report was released in September. Those two reports in particular go in great depth into the experience of the capital flows to these countries and to the workings of markets as these countries were influenced by those flows.

You say also there's no examination of banks in creditor countries. That's true. That's not the focus of this. One has got, when taking on a project of this nature, to define what the focus is going to be.

As you know, there's a lot of work going on in the context of the discussions of the international financial architecture, which go to the issue of the operations of the international banks and questions about the differential capital adequacy requirements on short-term lending by these banks versus longer term or syndicate operations.

Those are important issues. The fact that they are not in this paper is in no way, shape or form an indication of the extent of importance that we give to them. It is simply we wanted to look not at the details of the flows to these countries but at the way in which they reacted to them when the crisis ultimately developed.

There's an awful lot of material on each of these issues, as well, in the specific program documents for each of these countries, most of which are available on the IMF's website--the letters of intent, for example, for the programs with Korea, with Indonesia and with Thailand.

The question you raise about guarantees, just to make a point on that, is a critical one. It goes back to the comments that I made in responding to the question about the closure of the 16 banks in Indonesia. It's another one that we had to wrestle with very hard in deciding what was right, what was proper, what was going to be productive for the Korean authorities in their negotiations and discussions with the commercial banks.

To a certain extent, the horse was already out of the barn, as they say, on that issue. You will recall that in August of 1997 the Korean government in the person, I believe, of the deputy finance minister at that time, indicated that the government would cover the liabilities of the Korean banks. This was never passed into law but there is something in law called presumptive authority. The fact that an official of that rank in a government makes a statement of that kind gave creditors the right to expect that he was speaking with authority. There is a legal issue as to whether or not that guarantee could have been pressed, but it was there.

One can make the argument therefore that the guarantee offered by the Korean government in January 1998 was not new; it was simply a ratification of the guarantee that had been offered earlier.

On the other questions you mentioned--the cumulative impact of policies--that is one of the most difficult issues to come to grips with.

I think it's interesting, though, the point that you mentioned at the end, that Malaysia is, in fact, worse off when you look at many of the statistics for the Malaysian economic.

There is perhaps something behind that in terms of the way the Malaysian government in the end decided to approach the crisis and the fact that it was not along the same lines of the approach taken by the governments with which we were working intimately in the context of these programs.

QUESTION: My question concerns the success of the South Korean government in tightening monetary policy to support the currency. Do you think the Indonesia government should tighten its monetary policy now because the rupiah lately has been hit badly by the effect of the crisis in Brazil?

MR. BOORMAN: You're talking about today, current policy, I take it, not the experience with the monetary policy in Indonesia in the context of the program, if I understand your question correctly.

The Indonesian rupiah is weakening again, unfortunately. Whether or not that should be reacted to with a quick tightening of monetary policy I think goes to the question of the origin of the forces that are now driving that. Is it political developments and social developments in Indonesia? Very importantly, is it a spill-over from the episode in Brazil last week and some contagion from concerns in financial markets about developments in Latin America?

I think it's very difficult to make that judgment. It perhaps is too early to make that judgment and one would want to see how the situation develops, I think, before moving too aggressively on any policy to react to that. At some point, though, it may well be necessary.

MR. JING (*Maeil Business Daily*): I'd like to raise also a question about monetary policy.

You have mentioned that you have no apology about monetary policy by the IMF and you mentioned that high interest rates were key to stabilizing the currency in Korea and Thailand.

I think higher interest may be needed to those countries to stabilize their currencies but I think the basic problem is not choice between high and low interest but the more important choice is between how high interest rates should be set.

For instance, in South Korea overnight call rate was around 10 percent before the crisis and the IMF came in and requested the Korean government to raise the call rate over 30 percent. Why was it 30 percent, not 15 percent or 20 percent? That's a more important question for the policymakers from the viewpoint of local businessmen and local financiers.

Actually, those incredibly high interest rates hurt the whole economy and it produced a heavier blow to the real economy.

And you already admitted that recession has been deeper than expected. I think that may be one reason why the recession was deeper than expected.

And I think the IMF program, as you have mentioned, is too narrowly concentrated on removing the inflation-depreciation spiral but that spiral also conceals another spiral, for instance, in South Korea and in other countries probably. Higher interest rates, too high interest rates for the economy leading to more losing of confidence and more depreciation of their currencies. That may be one reason why the recession has been deeper than expected.

In stabilizing the currency there's also another factor other than high interest rates that you have to consider. That's rescheduling of the Korean debts in New York at the end of January last year. And some people say that that rescheduling was more important in stabilizing currency than higher interest rates. And what do you think of that?

MR. BOORMAN: Thanks. A couple of points. You will notice that perhaps the most extensive chapter in the study is on monetary policy because precisely of the kinds of questions that you raise. It is not an easy issue.

The extent to which and the time over which interest rates need to be raised and used to counter weakening of the currency is at least as much an art as it is a science. This is what central bankers get paid for--to have this feel of the markets and to understand and be able to work with markets in a way that uses interest rates in a way that instills confidence.

There's an interesting box on page 78 of the staff report that shows the experience and the use of interest rates by other countries. You'll notice in reading that box that an overnight rate of 30 percent is by no means an exceptional interest rate or exceptionally high in the context of a currency crisis. You'll find rates across the experience of countries that are much, much higher than that.

But given the challenge and the question about whether or not interest rates and monetary policy was used properly, you have to go to two other questions and the paper attempts to do that.

The first of those questions is how tight did monetary conditions become in the context of this interest rate policy? And the second one is what are the likely effects that that tightening of monetary conditions generally had in contributing to the decline in activity?

On the first of those questions, I think the evidence is particularly interesting that monetary conditions did not tighten dramatically, in Korea in particular or in Thailand, for example. Real money and credit growth in Thailand, I believe, declined slightly. In Korea, if my memory serves me, real money and real credit growth continued to be positive, in fact, throughout the episode. This is not a severe tightening of monetary conditions.

The other thing the staff tried to do then is to step back and say okay, given the way monetary conditions evolved, what contribution did they make to the weakening of the economy? And you'll see from that work that you cannot attribute much of the decline in activity and much of the recession to tight monetary conditions. That was not a factor. That was a result of many other things, including in particular, I think, certain dynamically unstable factors like the unhedged foreign currency exposure of the corporations, their short-term exposure, and so forth, that weakened the corporate position dramatically.

Let me say on this, though, the questions that have been raised outside are important questions and I do not mean to sound dismissive about them. There are difficult issues in knowing how to manage monetary policy and how to manage interest rate policy in the context of a crisis, and particularly in the context of a crisis that also stems from a weak banking and weak financial sector.

Those questions are legitimate. They need to be addressed. Good research needs to be done on them. But I think the experience here shows, through the ultimate stabilization of the exchange rates and the winding down then of the high interest rate policy which was used to bring about that stabilization, that monetary policy did work as the classic prescription tells you it will work in the context of a crisis such as this.

On your second question on the rescheduling, difficult to say what factor contributed how much at any one time. The rescheduling surely at that moment, at the end of December when the banks agreed to roll over their short-term exposures and then in January 1998 when the Korean authorities and the banks came to agreement on the restructuring of those obligations, was tremendously important in relieving pressure on the foreign exchange market. There is no question about that. It was an important part of it.

The extent to which one factor or the other contributed to the stabilization of the currency is very, very difficult to tell. You can see though, I think, in the episodes after the January restructuring when the won came under additional pressure and the authorities used interest rates, you can see a pattern of response there that suggests the importance of interest rate policy.

MR. BORSUK: Mr. Boorman, I would like to briefly ask a couple of questions specific to Indonesia and following up on the remarks you made in answer to previous questions.

One is related to the closure of the 16 banks in November of '97, which I think was the pivotal event in the beginning of the erosion of confidence in Indonesia.

You mentioned that one of the early lessons learned from the whole Asian crisis, and it's been one that a lot of people have mentioned a lot, is the need for transparency, greater transparency. But when the 16 banks were closed, wasn't the Fund concerned and already anticipating a problem because there was a lack of transparency about precisely what criteria were used to say that banks A, B and C had to be shut whereas banks D, E and F were okay when there were 50, 60, 120 other banks that were in a very poor state or at least believed to be shaky state? You mentioned yourself that it was no secret, the problems in the Indonesian banking system. Thank you.

MR. BOORMAN: We have to, I think, recreate a little bit the circumstances of that moment to come to grips with the important and I think perfectly legitimate question that you raise.

You know the history or lack of history in dealing with the problem banks in the Indonesian system in the early 1990s through the mid-1990s. There were not the closures that needed to take place, notwithstanding the fact that, as I said and you repeated, it was no secret that there were weaknesses in the system and in particular banks.

Judging the situation in a bank even in normal terms is not the easiest thing to do. It requires difficult valuations of the portfolio of the bank and the assets that lay behind the collateral of the claims of the bank.

Making those decisions in a moment of crisis is even more difficult and the line had to be drawn somewhere. The line in this case was drawn where the people who went in to help the Indonesian authorities survey the information that they had about the banks, bank by bank. They stopped at a point where it was perfectly clear that the 16 were well beyond any criteria that would suggest they could be left as operating entities. Surely beyond the 16 there were others that appeared very weak.

The ability, the time that was available, the information that was available to people at that particular moment to go further and begin to split hairs, if you want, on what was a good bank, what was a possibly survivable bank and then the 16 that clearly were not was difficult.

So the line had to be drawn at a moment of crisis and action had to be taken.

That goes a bit to the question of transparency. I'm not sure frankly at a moment like that what you can put out that would convince people that the 16th bank should have been closed and the 17th bank didn't have to be closed because I don't think, in fact, that was the reality.

There is an issue of transparency here, though, that is a little bit different than the one that you raised and I'd like to take the opportunity just to mention it because it is again one of the lessons from this experience.

That is the way that everyone involved, in the first instance the authorities and the policymakers in the country, but also the Fund, bilateral contributors and so forth, basically bring to the public knowledge about the specifics of the programs.

I think a case can be made that in the bank closure episode--I at least hinted at this in reaction to the first question--there was not enough public explanation about what was being done.

Going to your question, there was probably not enough public description of the criteria that were used to decide which banks would be closed and which ones may be permitted to remain open.

But much more broadly than that, and I would say this was a problem initially in all of the three crisis countries, there wasn't enough public explanation of why the crisis had occurred, what the critical elements were that had led to the situation, what needed to be done, what the results of initial inevitably painful action was going to be, but why it had to be that way to produce recovery, to produce stabilization, to produce eventually a renewal of growth.

This is a problem that confronts a lot of countries in crises like this. As I say, I remember the newspaper articles, magazine articles, television pieces in Korea in particular with people talking about the IMF program, quote-unquote. The fact of the matter is the general population or perhaps even well beyond the general population doesn't know what an IMF program is. The elements of it, the expectations for it, the process of it, needs to be explained to the population if you're going to bring the population along.

And we have good examples and not so good examples of the way in which country authorities handle this. I remember back to the early '90s the reforms in Poland and perhaps Czechoslovakia at that time, as well, where the then-finance ministers, Mr. Balcerowicz in Poland, Vaclav Klaus in Czechoslovakia, they were eloquent spokesmen and spent every weekend going out to towns and cities and on television in their countries basically saying, "This is what the program's about; this is what has to be done; these are going to be the initial results; this is why we have to do it in order to get kind of results and achieve the objectives that we're seeking."

There wasn't enough of that in Asia, not just on the banks but more generally in the context of these cases, in the early days. That changed certainly in November '97 in Thailand when Minister Tarrin came in. It changed certainly when President Kim Dae Jung was elected and took office in Korea.

MR. GOAD (*Asian Wall Street Journal*): Mr. Boorman, I'd like to do two things--go back to the very start of the crisis and the IMF's involvement in Thailand because you have mentioned in the report that the programs didn't work. The initial programs failed to stop private sector out-flows. For whatever reasons, there's no firm conclusions drawn in the report.

In the report you do say that in hindsight, because the programs didn't work, that means they were inadequately financed.

Going back to the situation in Thailand specifically and also more generally, do you feel that the second line of defense idea worked at all in these three countries? And specifically in Thailand's case, do you feel in hindsight that the decision of the United States not to participate and not to have ownership in a sense of a rescue effort contributed to not being able to reestablish confidence quickly?

There was a lot of discussion of that in Asia and certainly a lot of discussion in Thailand but at the time it was dismissed by the U.S. government and dismissed by the IMF as a nonissue.

MR. BOORMAN: A couple of points. First on facts, if I may. The so-called second lines of defense characterize the bilateral financing component of the programs with Indonesia and with Korea but not Thailand.

In Thailand, in fact, the support that was provided by the countries that were involved in the Tokyo Group was more in the nature of parallel financing, if I may use that phrase, in the sense that the money that was committed by those countries was committed to be disbursed and to be made available in concert with the IMF money. And, in fact, that is the way it was provided and those resources were disbursed.

So in the Thai situation I think it was a good arrangement. It did deliver resources to the Thai authorities and I think from that point of view it worked.

In the case of Korea and Indonesia, our conclusion is that those kinds of arrangements are problematic. And the reason we say that is because the private markets who are looking to see the amount of financing that will be available to a country in the midst of a crisis like this, the private markets need to be reasonably well assured that they understand the terms and conditions under which resources are going to be provided.

And I think it's fair to say that there was a lack of clarity in the conditions under which the second lines of defense that were provided in the context of the Indonesia program and the Korean program--the lack of clarity was such that the private markets couldn't assess very well the likelihood that that money would be actually available and would be disbursed to the countries. So we have concluded that there is an issue there.

I might add parenthetically on that that we have concluded that about our own operations, as well. Those of you who are familiar with the way in which the Fund operates know that typically a commitment of resources if made and that commitment is tranched. A certain amount of those resources are available when the program is approved and then additional resources are made available usually on a quarterly basis as the policy action of the authorities unfolds.

We attempted to deal with the lack of certainty that that process provides to private markets about the availability of resources by very heavily front-loading the resources that were committed and then disbursed to these countries. The size, as you know, the absolute size of the resources committed was unprecedentedly large but also the front-loading, the immediate availability of resources to these countries was also unprecedentedly large.

But there is a question about whether even that went far enough and those of you who might be familiar with the program that we have with Brazil know that we went one step even further and we floated, so to speak, the second tranche of resources that are available from the Fund to Brazil under the program, by which I mean after the program was approved and there was an immediate disbursal of resources, there is also a mechanism under that program where the Brazilian authorities can request that the second tranche be made available to them earlier than is programmed under the arrangement, again so that the markets see that there are substantial resources not just committed but potentially available to country, as well.

The second part of your question goes to the politics of the situation. Without going into great detail, you know the history perhaps of the Mexican program and the Mexican experience in late 1994-early 1995. Mexico being an important neighbor of the United States with a long border with the United States, the U.S. very much took the lead amongst the bilateral creditors in providing support to Mexico.

There was a sense, I think, that in Asia it was appropriate for countries, particularly the countries in the region, to be in the lead in assisting Thailand in this context. The political importance of that or the impact on the market is very difficult to judge. As the crisis unfolded and Indonesia was touched by it and then Korea was touched by it, of course the position and posture of the United States changed and they became actively involved, including in the second lines of defense.

QUESTION: You've maintained in the study that Thai fiscal policy is unlikely to have been a major factor behind the output decline. At the same time there are reports of credit squeeze. It seems to me that this part of your study is contradictory because early last year, Thailand used a tight monetary policy, coupled with tight fiscal policy and the tight fiscal policy may have aggravated the credit crunches of the economy.

So my question is how do you assess the result of tight monetary policy that's used at the same time as fiscal policy in Thailand?

And my second question is that it seems unclear to me that you have said that if Thailand imposes tight monetary policy aggressively and early, the pain will be less; would you please say specifically in the case of Thailand?

MR. BOORMAN: On your first question, there is an issue I think as to the extent to which there was a genuine credit crunch in these countries. The World Bank has done some work on this, including quite specifically in the context of Thailand, and the evidence is at best mixed. When the team that conducted this work surveyed Thai businessmen, businesswomen, and asked what the factors were that had interrupted their activity and their business in the early stages and on-going stages of this crisis, they did not, first and foremost, point to a lack of availability of credit. They pointed to lack of demand; they pointed to many things. But I think in a list of factors the availability of credit came out, at best, fourth or fifth.

That's consistent with the results of the work that was done by the staff here, which shows that there was in the context of Thailand at most only a limited decline in aggregate credit and aggregate money, even in real terms.

So I'm not sure that the anecdotal evidence about the credit crunch can be taken at face value.

Now let me say, though, quickly and add to that that there's no question that individual enterprises whose banks in particular might have been closed or might have been affected and who had to establish new banking relationships in the midst of a crisis would well have faced the situation much more difficult than in normal times in trying to assure the availability of full credit.

The second part of your question, I think what you're asking, but please clarify if I'm not correct, is if I think there should have been earlier and more aggressive monetary policy action, when that should have been.

As you know and as we have said and I think as the Thai authorities have said, we were advising the Thai authorities in late 1996 and early 1997 that they were facing very difficult pressures in the exchange markets and more generally in the economy and that action needed to be taken to deal with the policy weakening that was taking place.

One of the propositions that we were coming from at that time and one in which we have been even further convinced of is that--this goes to one of the previous questions that was asked about short-term capital flows and fluid international capital markets generally--we all know the benefits of open capital markets and I think even in the wake of this crisis, those benefits are still seen, still accepted and it is still accepted that it is best to open your markets.

On the other hand, what I might call the corridor of policy action, the extent to which you have to stay on the straight and narrow as a policymaker, is narrowed by the openness of capital markets. Mistakes can accumulate much more quickly and if those mistakes in policy aren't dealt with, the punishment from the markets is going to be more severe.

And so the demands on policymakers are much more severe than they might have been in the past before markets became as fluid as they are.

We were warning the Thai authorities in the context of our surveillance activities. If you ask specifically what could have been done earlier and more aggressively, it would have been a monetary policy tightening to deal with the attack on the bhat that took place in the spring of 1997.

There is also a question as to whether or not the bhat itself had to be adjusted in light of the weakening competitive position of the bhat, partly because of the appreciation of the dollar which had taken place, to which the bhat was tied; partly because of the overcapacity that had been built in the region on certain important Thai exports, like electronic goods, and so forth. There were fundamental questions being raised.

I think it is at least an open question as to whether or not the markets would have been calmed if the Thai authorities had made an exchange rate adjustment earlier and defended it with the needed additional policies, which would have included a tight monetary policy.

There are, I think, a good number of actions that could have been taken that might have avoided this crisis. This crisis did not have to occur. It occurred because of certain elements that developed in the international capital markets. It developed because of the vulnerabilities that were allowed to develop in these countries, particularly the short-term unhedged exposure, both in the banks and in the corporate sector. And, in my view, it occurred as well because of an insufficiently early and aggressive attack on those factors that were beginning to sow the seeds of this crisis.

MR. MING (*Korea Times*): Before I move on with my points that I would like to ask in three different areas, I would like to thank Mr. Neiss for arranging a contributed article for our new year's edition so that we could see your managing director's view and we could have it released to our readers in Korea.

My questions will be focussed on the appreciation of the Korean currency, which is posing a threat to the Korean export market recently, and the role of the Bank of Korea, which we presume is quite limited after the IMF bail-out.

And I presume that there will be a first quarter IMF review at the Finance and Economy Minister of Korea starting from the 20th of this month. And a lot of Korean politicians and some economic experts are saying now this is a time that the IMF should give more authority to the Bank of Korea and curb the continuous strengthening of the Korean currency, which is going to pose a problem to the domestic export sector.

And again I presume that all the policy decisions are eventually made from your headquarters where you are at the moment. I would like to know your views of the role of the Bank of Korea in the future. That would be my first point.

My second point is that you are well aware that there is a parliamentary investigation going on at the Korean National Assembly, which they look into cause and the process of Korea going through IMF period. And one of the most controversial factors is that Korean lawmakers investigation into when the Korean government contacted IMF headquarters for help and when it was released eventually.

The problem here is that a lot of people in the public believe that

Korean officials did not release information until the last minute, trying to cover the fact that they are getting external help from some organization in the United States. And if that is the truth, then they are the ones to be blamed. And if that is not the truth, there's no point having the investigation into the case.

Mr. Boorman, can you give precise details of what went on when IMF and Korean government was negotiating?

And my third point refers to your paper released today and it refers to page 13. Here on the fourth paragraph, it says, "Confidence was undermined by doubts about the commitment to the program as the leading candidates for the December 18 presidential election hesitated to publicly endorse it."

I presume the leading candidate is the incumbent president of Korea, who at a press conference said he wanted the terms of the IMF agreement to be renegotiated, rather than publicly endorsing it. Is Mr. Kim Dae Jung also to be blamed partly for the aggravation of the situation?

MR. BOORMAN: I think you broke the rules. That was the last question but you managed to make it the last four questions. Let me try to take each of them on to a certain extent.

First on the specifics of the release of information. There is an issue here which goes to the heart of a matter that we have been working very hard on in the last couple of years and that is transparency generally. Let me give you just one manifestation of it because it touches the experience in Korea directly.

That is the publication of international reserve figures by central banks and by countries generally. There are two issues that need to be addressed and are being addressed that are reflected in the Korea episode.

One is what are total international reserves? And there are difficult questions there about what resources, what monies are counted in international reserves and the Korean authorities were counting deposits in Korean banks as part of their international reserves. That was part of the $50 billion figure for international reserves in September 1997.

We have examined this issue and we have made proposals to our Board regarding the definition of reserves because if you count something like deposits of the central bank with its own banks and you have a banking sector problem, it raises questions about what we call the usability of those reserves. And that is an issue that has been taken more broadly to the international community.

As you may know, we have something called the special data dissemination standard, the SDDS, which is associated with a bulletin board operation where metadata and data for countries are provided. In the context of our responsibilities for that system, we have opened these questions about those kinds of issues regarding the definition of reserves. That's one aspect of it.

The other one is simply the frequency with which the public and the markets are informed about developments in reserves. We have been arguing here in the Fund for countries to release reserves on a weekly basis with a one-week lag.

It is our view that if international reserve data were put out with high frequency, the markets would see the way in which countries were managing their reserve position and to the extent that they were unduly trying to defend the currency, for example, in an unsustainable fashion by the use of reserves, ultimately, as happened in the Korean case, depleting those reserves completely, the markets would react in a more progressive manner, a more steady manner, rather than being shocked at some stage with the fact that reserves have been depleted and then having to react in a very aggressive and very destabilizing manner.

So that goes to the general issue I think you raised about information at that stage.

On the issue you raise about the Bank of Korea, I'm puzzled a bit by the way in which you state the issue in posing the question, that the Fund should give more authority to the Bank of Korea.

Well, it's not for the International Monetary Fund to give authority to any central bank. That is a matter of domestic tradition and domestic legislation.

Typically we do advise independence for the central banks so that they can conduct monetary policy distant from the political pressures of the day. This kind of independence has served many, many countries well and I think all countries need to examine the extent to which their central banks are independent and can conduct monetary policy in the fashion that I just suggested.

On your third point about--sorry I'm reversing the order--the point you raised about the appreciation of the won and the threat to exports. The current account in the balance of payments of the Korean economy has shifted absolutely dramatically over the course of the last year or so by a percentage of GDP that is probably larger than we have seen in the context of almost any other program the Fund has been involved in. It has had the result, as well, of leading to a large reaccumulation of international reserves, which is to the good.

But the other side of that coin is we are the International Monetary Fund. We have to be concerned about the competitive relations between all of our member countries, not just the competitive position of an individual country.

So the proper exchange rate for Korea is not a function solely of issues specific to Korea. It's also a function of the way in which Korea's or any other country's competitiveness affects the position of other countries and other countries in the region, as well.

And from that point of view it's a much more difficult issue than simply saying there may be a threat to exports. There doesn't seem to be a threat to exports to begin with but to the extent there may be--and I wouldn't call it a threat; I would call it careful examination of prospects for exports--one has to see the way that fits into the regional and the world context, as well.

Finally on your last question, on the president, I won't speak specifically to the position of Mr. Kim Dae Jung. The phrase that you see in that box refers to leading candidates, i.e., all three of the candidates for president at that time. And I think there is a question about the extent to which the public, reading the statements and hearing the statements of any of those three candidates, and even looking at the advertisements in the newspapers that those candidates were putting out in the context of their election campaign, the public would have certainly a right to question the extent to which each of those candidates was committed to the specifics of the program that had been agreed by the Fund.

To his great credit, I would say your president, immediately upon election on December 18, did clarify his position and publicly and forcefully expressed his full support for the program, which I think was an important turning point in bettering the situation which ultimately then stabilized in the course of January.

[Edited transcript]

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