

MR. DOOLEY: One of the things which has a lot to do with U.S. trade performance is the performance of the international monetary system. And given the recent crisis in Asia and elsewhere I thought I would direct my comments toward U.S. financial policy and, in particular, a response to financial crises around the world.

The U.S. government's aggressive response to the financial crisis that rocked Mexico in 1994 was an important watershed in the evolution of the international monetary system. For the first time since the debt crisis in 1982, the U.S. government and the governments of other industrial countries responded to a developing country's financial crisis with lending that was both timely and large enough to stabilize markets.

By any reasonable measure the policy was a success. The crisis was contained. Mexico recovered relatively quickly and was able to repay its obligations ahead of schedule.

The down side of the more aggressive approach to crisis management emerged later with a series of crises in Russia, Eastern Europe, and Asia. Simply put, private investors took comfort from government commitments to act quickly and decisively to limit the cost of financial crisis through official

lending. Such policy allows private investors to liquidate their claims on a country on better terms that would be available without the government backstop. This does not mean that all private lenders are fully insured. Clearly there have been painful losses to investors following the recent crisis. When private investors rush to exit, some are still left behind. But, on average, the cost of the crisis to international investors has been reduced, and they have responded with more, and less careful lending.

If we are to continue to enjoy the full benefits of trade with emerging markets, the sequence of crisis, bailouts and more crisis will have to be broken. The continued growth and vitality of emerging markets will require open and competitive financial markets. A financial crisis can generate very large reductions in economic activity in these markets.

A typical crisis, if there is such a thing, reduces growth in developing countries by about five percentage points for four years. This is an important threat to U.S. exports and the availability of key imports and, clearly, the stability of the international monetary system.

Aggressive official lending has helped contain these costs, but has encouraged reckless borrowing, leading to more and frequent crisis.

In a recent paper I argued that the only approach to this dilemma that is both feasible and effective is for creditor governments to require concessions by private lenders as a condition for their loans to debtor countries. This is sometimes called bailing in the private sector. And, through the IMF, creditor governments have recently made some very small steps in this direction.

If this approach is to have a chance of success, however, creditor governments, and especially the United States, must be willing to finance debtor countries for an extended time period while debtor governments negotiate with their private creditors from a position of strength.

It follows that creditor governments in the IMF will have to be much more selective in choosing debtor countries that can effectively utilize financial assistance.

COMMISSIONER KRUEGER: Thank you very much.
And Reuven Glick.