

# Conference ponders global outlook, financial crises, and effects of capital account liberalization

Assaf Razin has been writing about the promise and the perils of international economic integration for over three decades—long before globalization became a buzzword. Razin turned 60 this year, and his colleagues, collaborators, and friends marked the milestone by throwing a conference in his honor in Tel Aviv on March 25–26.

What were the highlights of the conference? Jacob Frenkel, Leonardo Leiderman, Paul Krugman, and Anne Krueger offered colorful, and sometimes contradictory, assessments of the world economic outlook. Krugman also sketched what the next generation of financial crises might look like. In addition, Andrew Rose evaluated the interest rate defense of currency pegs, and Barry Eichengreen and Charles Wyplosz offered a fresh assessment of the growth effects of capital account liberalization.

**Shifting global outlook**  
Jacob Frenkel of Merrill Lynch International launched a panel discussion on the global outlook with a cautiously optimistic assessment of the U.S. outlook for 2001–02. Frenkel noted that, like Mark Twain's description of Wagner's music ("it's better than it sounds"), the U.S. economy is in better shape than it appears. The "slow-down feels like a recession" because of the sharp contrast with the strong growth in the preceding years. He predicted that the United States would easily avoid a recession this year. Consumer spending, he noted, has started to recover; housing starts have remained robust; and produc-

tivity growth remains positive. According to Frenkel, downward revisions of forecasts of the U.S. economy reflect, to some extent, the "filtering of psychology into forecasts," as forecasters react to the sharp declines in the U.S. stock market. These reactions are more than warranted by U.S. economic fundamentals, including the likely course of U.S. monetary and fiscal policies.

The next panelist, Leonardo Leiderman of Deutsche Bank, struck a more pessimistic note. In his view, the U.S. economy was in "recession territory," and growth prospects for 2002 were anemic as well (see chart, page 130). As evidence in support of his forecasts, Leiderman pointed to the slowdown in all components of domestic demand and to the signals from the index of leading economic indicators.

After listening to Frenkel and Leiderman, Paul Krugman of Princeton University remarked that "we've just heard a bad forecast from an Israeli economist; the trouble is, we don't know which one." Krugman's own forecast for the U.S. economy was closer to Leiderman's. While agreeing with Frenkel that U.S. supply-side performance had been strong, Krugman suggested that this did not insulate a country from the business cycle, as shown by the economic debates following strong growth in the United States in the 1920s and Japan in the 1980s. As in these earlier episodes, strong U.S. growth in recent years has been accompanied by a bubble in financial markets and an overhang of bad investment. Krugman also questioned the "theoretic" about just-in-time inventory management techniques, won-

Assaf Razin at 60

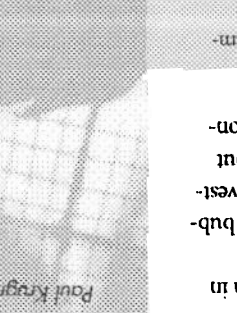
Like other peripatetic Israeli scholars, Assaf Razin has, over the course of his career, combined an academic affiliation at home (Tel Aviv University) with visiting positions at several U.S. and European institutions, including several stints as a visiting scholar at the IMF. At the conference in his honor, Razin briefly summarized the highlights of his illustrious career—one in which he has written a dozen books, edited a dozen others, and published over 100 articles. He observed that a rejected paper in 1975 led to his first book on globalization—a subject that still fascinates him. *A Theory of International Trade Under Uncertainty*, written with Elhanan Helpman, argued that as capital markets became more integrated, there would be a strong tendency for countries to specialize according to their comparative advantage. Three subsequent books continued to explore the implications of global integration. *Fiscal Policy in an Integrated World Economy: An Intertemporal Approach*,

written with Jacob Frenkel in 1987, looked at the dynamics of the current account in a flexible price world; *International Taxation*, written with Frenkel and Fritzi Sadka, examined the constraints that globalization imposes on the conduct of fiscal policies (the main problem, according to Razin, is a "race to the bottom" among national tax authorities in a globalized tax market); and, more recently, *Flows, Capital, and Finance: International Effects (good and bad) of globalization*. Razin, noting that in the Jewish tradition every one lives for 120 years, said he viewed this conference on his sixtieth birthday as "a wonderful break between semesters." Also, deflecting the praise heaped on him during the conference, he quipped that he wished his parents could have been on hand: "my father would have liked to hear all this praise, and my mother would have believed all of it."

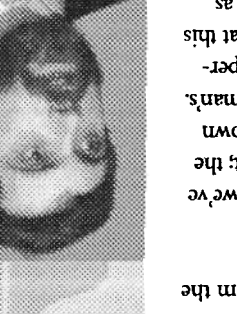
Assaf Razin



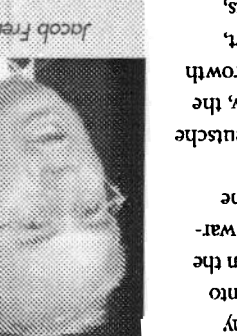
Jacob Frenkel



Paul Krugman



Leonardo Leiderman



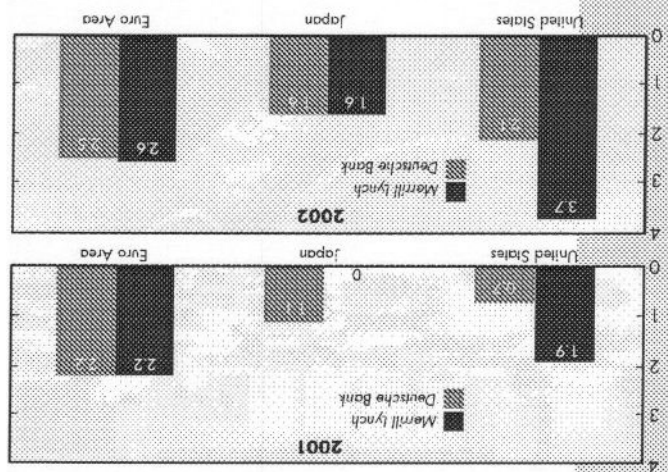
Andrew Rose



Charles Wyplosz



dering what accounted for the huge buildup in manufacturing inventories if these techniques were working as advertised. Leiderman and Anne Krueger of Stanford University discussed the likely impact of the U.S. slowdown on private-sector growth forecasts.



Anne Krueger

other countries. Leiderman noted that the decline in U.S. import growth to an estimated 2 percent for 2001—far below the nearly 15 percent import growth of recent years—would have the predictably adverse impact on Mexico and many Asian economies. A slowdown could also trigger an increase in U.S. protectionism, Krueger warned, noting that protectionist pressures had not diminished despite the strong economic growth of recent years. The resolution of ongoing trade disputes, such as the one involving softwood lumber imports into the United States from Canada, would test the “free trade credentials” of the Bush administration, she said.

**Financial crises**  
 A paper by Krugman—“Crises: The Next Generation?”—provided a narrative history of the literature on financial crises, highlighting the “dismartening fact” that each wave of crises elicited a new style of models that made sense of the crisis “after the fact.” Against this backdrop, he attempted “to get ahead of the curve” by sketching what the next generation of crisis models (the fourth such) might look like. According to Krugman, the next generation of crises may affect not currencies but asset prices more generally. The mechanisms for speculative attack and self-fulfilling pessimism identified in models of currency crises apply to stock markets as well. In the currency-crisis models, a disorderly devaluation of the currency raises the value of firms’ foreign currency debts, thereby lowering their net worth and forcing them to curtail their investment. Krugman argued that one can tell a similar story in which

**Capital mobility and growth**  
 Though economic theory predicts that international capital mobility should have favorable effects on economic growth, “the data do not speak loudly” on this issue, according to Barry Eichengreen of the University of California, Berkeley, and Charles Wyplosz of the Graduate Institute of International Studies, Geneva. In joint work with Carlos Artea, they reviewed the financial literature on the impact of capital account liberalization on growth and indicated that the previous findings have been not only contradictory but also sensitive to the set of countries considered, the time period studied, and the econometric method used. Their own investigation yielded some support for the view that “the sequencing of reform shapes the effects of capital account liberalization” but, they cautioned, “we need to better understand [the] how and why” of this result. ■

**Member’s use of IMF credit**  
 (in million SDRs)

During	March 2001	January–March 2001
General Resources Account	163.80	3,499.58
Stand-By	105.00	3,440.78
SRF	0.00	2,349.57
EFF	58.80	58.80
CFE	0.00	0.00
PRGF	94.86	167.29
Total	258.66	3,666.87

1,253.33  
 86.81

SRF = Supplemental Reserve Facility  
 EFF = Extended Fund Facility  
 CFE = Compensatory Financing Facility  
 PRGF = Poverty Reduction and Growth Facility  
 Figures may not add to totals shown owing to rounding.  
 Date: IMF Treasurer’s Department

Prakash Loungani  
 IMF External Relations Department

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