Introduction to Special Issue: Symposium Part II

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IMF CONDITIONALITY AND PROGRAMME OWNERSHIP IN DEVELOPING AND EMERGING ECONOMIES: IMPLEMENTATION AND RESEARCH AGENDA

The purpose of the special issue is to contribute to the ongoing debate on the effectiveness of IMF conditionality and structural reforms, as well as the issues regarding the implementation of programme ownership in practice. In this regard, the first volume of the special issue, which was published in the September 2004 issue, introduced five papers dealing with issues of conditionality, ownership, and programme performance in developing and emerging economies. The second issue presents three additional papers that complete the special issue. The special characteristic of this second issue is its focus on emerging and transition economies, rather than developing economies.

In the first paper, Ayse Evrensel examines the performance of 19 emerging countries that received IMF-supported stabilisation programmes during the 1971–1997 period. Her study is important because it studies the effectiveness of conditionality in emerging countries, while previous studies mainly focus on developing economies. Compared to non-programme countries, she finds that emerging economies with Fund programmes had periodic macroeconomic crises and implemented inconsistent macroeconomic policies. In addition, she finds evidence of temporal moral hazard, which indicates that, as countries receive subsequent programmes, they tend to follow more inconsistent policies during inter-programme years. She concludes that the complex relationship between the IMF and emerging countries should be examined based on the decision-making process that takes place both at the IMF and in programme countries. She therefore emphasizes the need for additional research on these issues. Her results from emerging markets may have implications for the transition economies of Central and Eastern Europe and the former Soviet Union.

In the second paper, Eke and Kutan investigate whether IMF programmes are effective in the transition economies of Bulgaria and Poland. They first present historical evidence about the implementation of Fund programmes in both countries during the 1990s and compare their outcomes. Although Poland did not sign new programmes with the Fund after 1994, IMF programmes are still in effect in Bulgaria. They also conduct empirical tests regarding the effectiveness of IMF programmes. The results suggest that IMF programmes were more effective in Bulgaria than Poland, especially in reducing the probability of inflation crises. In interpreting their results, they caution the readers, because the effectiveness of IMF programmes depends on a host of factors, including the nature of IMF programmes and policies, the commitment of the country's officials to perform these programmes, the degree of social and political stability, as well as external and transition-related shocks.

The next paper investigates the effectiveness of fiscal structural adjustment programmes in an economy that has been suffering from moderate inflation and political instability for some time. Ebru Voyvoda and Erinc Yeldan investigate the impact of a recent IMF fiscal adjustment programme on growth and welfare in Turkey. In May 2001, Turkey and the IMF signed a new program with the main focus on the long-term sustainability of fiscal adjustment with particular emphasis on budgetary discipline and fiscal surplus. Using an overlapping generation model, the authors simulate the effect of the programme on production, investment, growth and welfare. They find that an alternative policy that focuses on increased public spending on education would produce more sustained economic growth than the 2001 IMF programme, which focused on the stabilisation of debt dynamics through fiscal surpluses. An important lesson here is that the involved parties need to evaluate the trade-offs associated with the implementation of different fiscal adjustment programmes and better assess the particular constraints faced by programme countries. For example, Turkey has insufficient funds for public education, which may hurt economic growth.

An important research area that is not explored much in the literature is to examine the possibility of creditor moral hazard in equity markets. Most studies of moral hazard focus on bond markets. Several observers have suggested that the Fund-support to Indonesia, Korea, and Thailand during the recent East Asian crisis may have provided additional implicit guarantees to investors, which would motivate them to take excessive risks. Implicit guarantees to investors indicates domestic moral hazard, which implies that financial intermediaries or their owners were protected by implicit or explicit government guarantees against losses, which reduces financial firms'

incentive to manage risk. Domestic moral hazard could become more pronounced, if Fund-support to crisis countries signaled the continuation of domestic implicit guarantees. In countries' financial sectors with domestic creditor moral hazard, does an expected IMF support cause an additional type of moral hazard? This kind of moral hazard could be called IMF-induced creditor moral hazard. Besides Asia, recent financial crises in Turkey, Russia, and elsewhere suggest that the frequency of the IMF's involvement in emerging markets is likely to increase in the future. It is therefore important to understand whether such moral hazard exists in emerging markets. Evrensel and Kutan (2004a,b,c) provide some initial tests of the creditor moral hypothesis.

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