CONGRESS OF THE UNITED STATES

JOINT ECONOMIC COMMITTEE

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PRESS RELEASE

For Immediate Release
August 13, 1998

Press Release #105-162
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ASIAN FINANCIAL MELTDOWN SOURCES IDENTIFIED
— IMF LENDING PRACTICES PERPETUATE COUNTERPRODUCTIVE INCENTIVES —

WASHINGTON D.C. – Joint Economic Committee Chairman (JEC) Jim Saxton (R-N.J.) today released a new study finding a combination of perverse incentives is a key contributing factor to recent financial crises in emerging economies, including Asia.

The report, "Financial Crises in Emerging Markets: Incentives and the IMF," finds that incentives to overextend credit (created by a combination of government guarantees, risky lending opportunities and low levels of owner-contributed equity capital) often produce conditions resulting in financial crises.

"Recognizing and correcting these counterproductive incentives is key to preventing future financial crises," said Saxton. "The weak financial structures in many affected nations suggest that recovery will be a slow and painful process in many cases."

The JEC study shows such incentives played a key role in the creation of current financial problems plaguing many emerging economies. The impact of incentives is similar to what troubled U.S. savings and loan and banking industries in the 1980s and early 1990s.

The JEC study explains how these problems are more severe in many emerging economies today. The study demonstrates that recent IMF lending and prospects for its future lending serve to reinforce existing counterproductive incentives and create an additional layer of risk subsidies at the international level.

"Recognizing these perverse incentives is a prerequisite for taking corrective action rather than reacting to events," Saxton said. "One appropriate response is to adopt policies to limit the moral hazard problem. This could entail limiting additional IMF funding. But corrective action could also include proposals to modify these perverse incentives such as requiring IMF lending rates to be more market-determined and ensuring more transparency on the part of the IMF."

Saxton has sponsored the IMF Transparency and Efficiency Act, H.R. 3331, to provide these reforms. The new study can be obtained by contacting the JEC at (202) 224-5171 or by viewing the committee's website at http://www.house.gov/jec.

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