Foreword by the Commonwealth Secretary-General

When Commonwealth Finance Ministers met in Canada in September last year, the world economy was in the throes of possibly its worst ever crisis since the Great Depression of the 1930s. In their Ottawa Statement on the Global Economic Crisis, they therefore agreed that the international community should respond swiftly to preserve the stability of the international economic and financial system and protect the hard-won gains of economic liberalisation in many parts of the developing world. Ministers made several specific proposals for crisis prevention and management. In particular, they stressed that the present international monetary and financial system needs to be reformed and that the development of a new international financial architecture should be pursued vigorously. They proposed that reforms of the global monetary and financial system be agreed by the year 2000 at a global meeting involving broad-based representation from industrial, emerging and other countries at different stages of development.

The Commonwealth Finance Ministers based their discussions on the Report by a Commonwealth Expert Group, which I constituted in response to their request in September 1997, for a study on the lessons to be learned from the East Asian crisis and on how countries could be protected from the destabilising effects of market volatility, including those resulting from speculative activities. The Group, which brought together eminent economic and financial experts from all regions of the Commonwealth, and was chaired by Mr Chris Liebenberg, former Finance Minister of South Africa, completed a challenging task in a remarkably short period of time, holding two meetings in London in June and August 1998.

In drawing lessons from its analysis of the East Asian crisis, the Expert Group came to the conclusion that a comprehensive strategy for dealing with financial crises needs to be directed at four levels: national action to reduce the likelihood of future crises; regional actions to limit damage and contagion in the immediate neighbourhood; international actions to co-operate effectively in preventing and/or managing future crises; and strengthening international regulatory frameworks in order to enhance global stability.

The Group's recommendations for effective crisis prevention include increasing transparency of market operations; strengthening surveillance and peer reviews; regulating and/or taxing capital inflows and outflows; and the use of counter-cyclical policies. While the Group prefers the use of market-based measures to regulate capital inflows, it believes that it may be necessary for countries to consider capital controls, on a temporary basis, in the event of a serious crisis where the costs of any resulting distortions are likely to be lower than the alternative of an economic slump. On crisis management and containment, several proposals are made to improve the effectiveness of international financial institutions (IFIs). In particular, the Group recommends that the scale of their existing facilities and resources should be enlarged significantly, and that appropriate conditionality needs to be designed in stabilisation programmes in order to restore stability and market confidence without damaging growth in the countries affected.

The Report makes a strong case for orderly debt workout procedures with private creditors being required to continue to lend in crisis situations. This together with temporary suspension of payments would bring about the rapid resolution of crises, while reducing the scale of official financing required. The Report emphasises the need for concessional assistance for low-income countries which are hit by rapid reversals of capital flows and lack alternative sources of funding in crisis circumstances. It also stresses the importance of the World Bank, other IFIs and bilateral donors acting early and on a sufficient scale to help affected countries deal with the social implications of financial crises. Finally, the Report addresses the need to fill regulatory gaps in the international system particularly in relation to short-term bank loans and easily reversible short-term portfolio flows. It also draws attention to the potential role of regional arrangements and mechanisms in crisis prevention and management, which can play an important "mezzanine" role between national and international institutions. This is an area which has not received adequate recognition in most current proposals and therefore reflects a serious gap in the international financial system.

Since the Expert Group completed its work, developments in financial markets – especially the most recent crisis in Brazil – have underscored the importance and relevance of its key conclusions and recommendations. I hope this Report will be widely read and believe it will make an important contribution in influencing both debate and action to build the new financial architecture which the global economy needs so urgently as we enter a new millennium.

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