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THE AMERICAN COLLEGE OF GREECE MAGAZINE

Dr. Miranda Xafa

Deree Alumna; Outgoing Alternate Executive Director, IMF

THE AMERICAN COLLEGE OF GREECE MAGAZINE

contents

also

Commencement by the numbers

614 number of students who graduated from Deree and the Graduate School in June 2009

members of the graduating class who received awards at Commencement 2009 **5**

17 number of countries represented in the graduating class of 2009

kilos of recycled confetti used at the end of the ceremony in 2009 **18**

3 number of honorary degree recipients

approximate number of family members and friends of the graduates who attended Commencement 2009 **10,000**

23 number of students at Commencement 2009 who graduated with Highest Distinction from the Graduate School and Deree

number of students who graduated with High Distinction from the Graduate School and Deree **41**

23 number of students who graduated with Distinction from the Graduate School and Deree

members of the Deree Symphony Orchestra that performed during Commencement 2009 under the direction of Dimitri Toufexis **50**

6 number of Junior College students who graduated with Honors

number of balloons dropped from the stadium's ceiling at the commencement ceremony **8,000**

12 members of the Deree Choir that performed during Commencement 2009 under the direction of Maria Kokka

5,000 number of copies of the commencement program distributed

A Bird's-eye View of the Global Crisis

By **Harilaos H. Daskalothanassis**

For five years, the post of Alternate Executive Director of the International Monetary Fund has afforded Deree graduate Miranda Xafa a bird's eye view of the global economy, which for the past year has been going through its roughest patch since the Great Depression of the 1930s. Yet, Xafa, who studied economics at Deree before earning her Ph.D. at the University of Pennsylvania, is also intimately acquainted with the workings of the Greek economy and the Greek political system. In the early 1990s she served as economic advisor to then-prime minister Constantine Mitsotakis, whose government was the first to attempt wholesale reforms of the Greek economy, mainly by trying to wean Greek business away from its dependency on the bloated and inefficient state sector. In an interview with ACG Magazine, as she prepared to leave the IMF for a senior post in a Geneva-based private asset management company, Xafa spoke about the current global crisis, defended the role the IMF has played in the global financial system, and reminisced about her years at Deree.

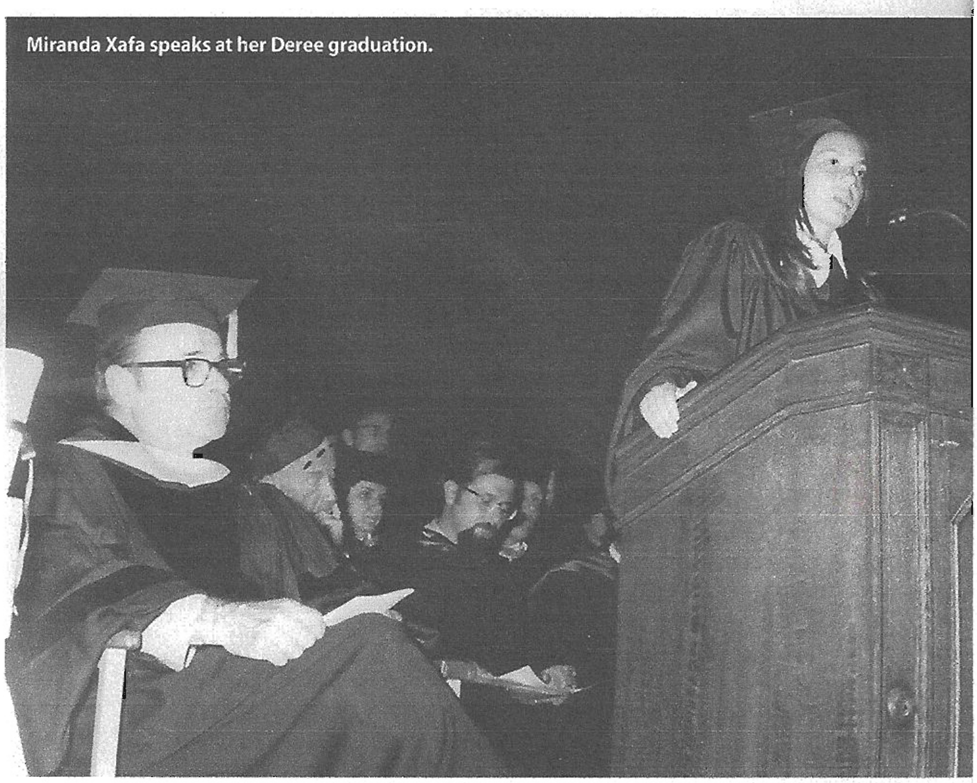
There is a feeling emanating from various government and business sources that the worst part of this recession is over and things might be picking up. Is that true from your perspective at the IMF? What are the latest projections regarding the current slump?
There are some signs that the rate of global output decline has moderated, after two quarters of unprecedented economic contraction. But we are not yet out of the woods. Recovery will be slow because deleveraging in the financial system still has a long way to go. Until banks are recapitalized and their balance sheets are cleaned up of impaired assets estimated at \$2.8 trillion, they will continue to exert downward pressure on economic activity. There is a negative feedback loop between the financial system and the real economy, as the global recession puts further pressure on bank balance sheets and further discourages lending. Despite massive fiscal stimulus and unlimited liquidity provision by central banks, the IMF forecasts that global output will decline this year for the first time in the post-war period and recover only modestly in 2010.

What was the cause of the crisis? A failure of regulation or the global imbalances that kept interest rates low?
The crisis was caused by a failure of both regulation and market discipline. In the absence of this failure, the crisis would not have happened even though the global imbalances – a euphemism for the large U.S. current account deficit and corresponding surpluses of China and oil-producing countries – would have persisted. Conversely, if the global imbalances had somehow been corrected, i.e., global savings were redistributed from the surplus to the deficit countries, the world interest rate would be unchanged and the global crisis would still have happened. The failure of regulation was multiple, as it permitted the expansion of bank activities without a corresponding increase in capital, and it failed to take liquidity risk into account. At the root of the crisis were the government-sponsored U.S. mortgage giants Fannie Mae and Freddie Mac, which were allowed to expand their lending with little oversight, based on social priorities. At the same time, there was a failure of market discipline, as competitive pressures drove credit spreads to their tightest level when systemic risk was at its peak.

Does the crisis signal a failure of capitalism?
Not at all. Markets need to be based on solid institutional foundations. What we are witnessing is not a failure of capitalism or free markets. It is a failure of poorly regulated markets.

Do you foresee a significant and lasting shift towards greater regulation in the new financial world order that will emerge once the global recession fades? What changes do you consider necessary?
There is a need to redefine the perimeter of regulation to include all systemically important institutions and markets. What we have seen in this crisis is an unexpected and undesired increase in banks' balance sheets when they had to explicitly recognize their off-balance sheet exposures. This "shadow banking system," which was unregulated, contributed significantly to the crisis. Non-banks also played a role, as the rescue of insurance giant AIG demonstrates. Off-balance sheet derivatives also caused much distress to counterparties in the aftermath of Lehman's failure last September. To ensure a consistent approach to regulation, the information collection framework should be monitored though a globally coordinated mechanism, with a key role to be played by the IMF. At the same time, however, it is important to avoid a rush to regulate that could stifle innovation and impose unnecessary administrative burdens.

Last April, the G20 agreed to triple IMF resources to \$750 billion. How will this help address the crisis?
IMF staff analysis indicates that refinancing needs of emerging market countries are set to rise from \$1.7 trillion in 2008 to \$1.8 trillion in 2009 and \$2.0 trillion by 2012. There is no way these debts can be rolled over during the current global financial crisis, when banks and institutional investors are trying to reduce the risk and leverage in their portfolios to maintain capital adequacy despite the losses they have suffered. This fact underlines the need for a significant increase in Fund resources to ensure their adequacy as countries are queuing for large loans from the Fund to avoid a painful crisis that could force them to default on their external debt obligations.


Miranda Xafa speaks at her Deree graduation.

Some critics connect the Fund with a merciless globalization that helped propagate the current crisis. How does the IMF respond to the challenges today?
First, I would observe that globalization – the free movement of goods, services, and capital across national borders – has lifted out of poverty hundreds of millions of people in the developing countries. In fact, globalization has done more to alleviate poverty in the 20 years since the collapse of communism than 65 years of poverty-reduction efforts by multilateral development banks and bilateral donors in the post-war period. Surely the lesson from the current crisis is *not* to reverse financial

verely affected the Greek economy. The IMF forecasts a decline in output this year, while the high and rising public debt burden provides no room for expansionary fiscal policy to offset the output decline. During the past upswing, rapid growth promoted convergence of Greece's per capita incomes with the Euro area average. But the benign global environment masked a deterioration in competitiveness and an increase in both public and external debt levels. These imbalances now call for corrective action to reverse both the unsustainable rise in debt and the erosion of competitiveness in order to lay the foundations for sustainable growth. In its absence, Greece risks getting trapped in a low-growth equilibrium.

You were an advisor to Prime Minister Constantine Mitsotakis some 18 years ago, and you know first hand the difficulty of introducing reforms into the Greek economy. Reform is difficult in almost every country because it implies sacrifices, yet many countries have managed to pull it off. In your opinion, what is it that makes reform in Greece so much more difficult than in those other countries?

The political system in Greece is not conducive to reforms. There is no clear separation of powers between the executive, legislative and judicial branches of government. Parliament is a rubber-stamping body that approves all legislation submitted by the governing party. Dissenting voices are dropped from the ballot or even expelled from the party. The cabinet consists of MPs who need to worry about their re-election. Governments are guided by opinion polls, and concern about the political cost of reform efforts weighs heavily in the decision-making process. They tend to support populist policies that keep resources trapped in inefficient activities, in the name of a misplaced social policy that discourages growth and innovation. Think of how much Olympic Airways has cost taxpayers and how long it took to privatize it. When countries face problems that require long-term solutions, such as pension reform, the main political parties get together and agree on needed reforms. In Greece the planning horizon is up to the next election at best, and neither of the two main parties plays a constructive role while in opposition. The politically powerful public sector unions, whose members enjoy job security at taxpayers' expense, also are a key obstacle to reform. Given these difficulties, a surprising number of reforms were

liberalization and restrict capital flows. On the contrary, what is needed is a shock absorber that can soften the impact of a "sudden stop" in private capital flows. Accordingly, the IMF is adapting its policies in response to the global crisis. The Fund has injected flexibility into its lending framework by creating a new instrument to provide large, upfront financing on a precautionary basis, and to better tailor conditionality to country circumstances. Countries with solid fundamentals and strong policies now have access to IMF financing on demand, with no conditionality, to address actual or potential balance of payments pressures. Together with increased lending limits, the new precautionary Flexible Credit Line provides insurance that helps strengthen market confidence about the country's ability to meet rollover needs and thus avoid a crisis. Mexico was the first country to benefit from the FCL last March, with a $47 billion loan – the largest in the IMF's history – followed by Colombia and Poland. In addition, the IMF is working with the Financial Stability Board on a set of leading indicators, in an effort to come up with early warning signals of possible future crises on a country-by-country basis.

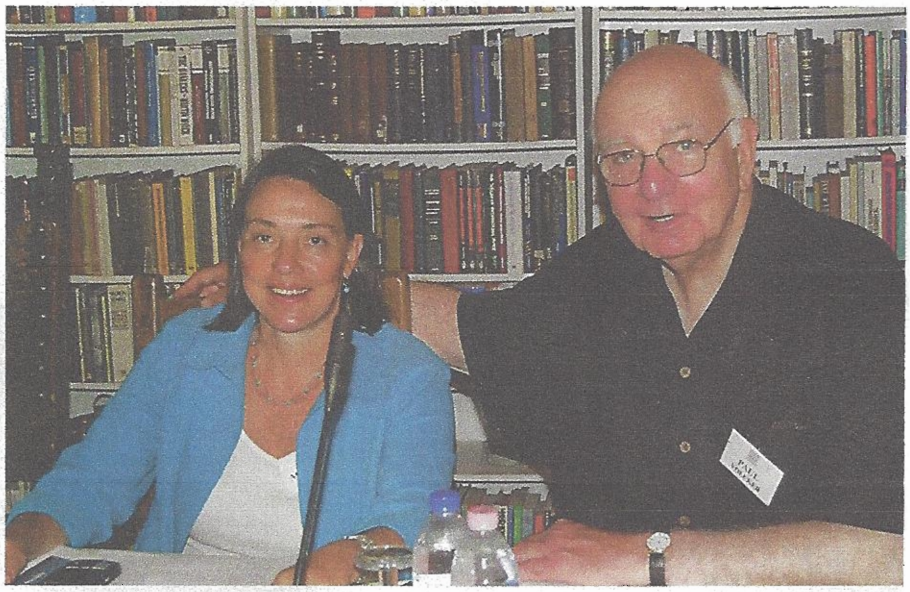
In the past, the IMF has been criticized for demanding austerity measures that are excessively harsh, in order to agree to assist faltering economies. Do you think the criticism has any validity?

No critique of the Fund is more misguided than the austerity critique. IMF programs make austerity *less* likely. Let's get the facts straight: Countries request IMF assistance when they are in deep financial difficulty. These countries have typically lost access to capital markets, so the Fund is the lender of last resort. By providing financing that would otherwise be unavailable, IMF loans allow a distressed debtor country to tighten its belt less than otherwise. The economic policy conditions attached to IMF loans are instead of the stricter discipline that market forces would otherwise impose. During the 1997 Asian crisis, for example, Korea and Thailand were facing outright default and a prolonged free fall in their currencies – a far more damaging outcome compared to IMF "austerity." The austerity critique stems from the fact that the IMF provides a convenient scapegoat when politicians confront their populations with a tighter budget. "The IMF forced us to do it!" is the familiar excuse when governments cut spending and subsidies. The critique confuses correlation with causation: Blaming the IMF for the reality that every country must confront its budget constraints is like blaming the Fund for gravity.

Recently you were in Greece as part of an IMF delegation that delivered some harsh judgments on the Greek economy and prescribed solutions that are regarded by some in Greece as too severe. How serious is the situation in Greece? Is the country really on the verge of bankruptcy?

The deepening global downturn has se-

Previous page: Miranda Xafa with Prime Minister Constantine Mitsotakis when they were introducing the first radical reforms of the Greek economy.
Right: Xafa with Leslie Lipschitz, director of the IMF Institute.
Below: In Rome with Barack Obama advisor and former chairman of the Federal Reserve Bank Paul Volcker earlier this year.



implemented, or at least initiated, by the Mitsotakis government that I am proud to have served.

Are you hopeful about the future of the country? Do you think Greece will manage to modernize and therefore protect and improve the standard of living of its people?
Greece has a very entrepreneurial and dynamic private sector – a great asset! Sectors with little government involvement, such as shipping, are global leaders. Despite the bloated and inefficient public sector, the country is modernizing as inventive people find ways around the red tape and take advantage of E.U.-mandated liberalization, for example in the telecoms sector. Many young people choose to study abroad or at the American colleges in Greece – whose diplomas are not recognized by the Greek state – rather than in the Soviet-era Greek university system.

Did participation in the euro area save Greece from a catastrophic downturn during this crisis?
The euro offers a strong shield, by providing easy access to financing from the ECB and by eliminating the currency risk that plagues neighboring countries like Hungary and Romania, which are members of the E.U. but not the euro area. These countries have recently resorted to IMF financing because they lost access to capital markets despite the fact that their fundamentals were somewhat stronger compared to Greece.

What have been your duties at the IMF and what kind of decisions were you called on to make in your capacity as its alternate executive director?
The 24-member Executive Board takes care of the daily business of the IMF. Together, these board members represent all 185 member countries. Large economies, such as the United States and China, have their own seat at the table, but most countries are grouped in constituencies representing four or more countries. The board discusses everything from the annual health checks of member countries' economies to broader policy issues affecting the global economy and financial system. It is also the body responsible for approving IMF loans to member countries. Decisions are usually taken by consensus, although sometimes a formal vote is required when issues are divisive, as they were in the early 2000s with respect to IMF lending to Argentina.

What talents does your job require?
Besides a solid background in economics, the job requires good writing skills, ability to react quickly and participate in the debates at the board, staying on top of issues and developments, and ability to work well under pressure.

What will be your new position in the private sector?
I will be joining IJPartners, a just-launched asset management company based in Geneva, as senior investment manager and member of the Advisory Board. IJ stands for Informed Judgement - a new approach to the challenges of preserving, growing and using wealth responsibly across generations. The company brings together a team of highly qualified professionals from different backgrounds. I look forward to working with them and joining an exceptional Advisory Board that includes Nobel laureate Robert Mundell.

What did you study at Deree and how did it contribute to your success as an economist and executive?
I studied economics in an intensive three-year program including summer courses at Deree. This enabled me to get high scores on my GRE exams and get accepted into the Ph.D. program in economics at the University of Pennsylvania. My courses at

Deree taught me how to learn and think for myself – a skill that is far more important than memorizing facts and figures.

Were you a good student? Were you active in student affairs?
I was pretty good, but did not get straight A's because I focused on the courses I liked the best. As an economist, I learned to equalize returns at the margin! I was more interested in tennis and water skiing than in student affairs back then.

What was your favorite class?
Economics.

Your least favorite?
Biology.

Your favorite professor?
Anthony Kefalas, who enriched his economics classes with cultural, social and political background on the United States based on his own experiences as a student there.

What was your favorite place on campus?
The cafeteria, where all the networking takes place.

Did you make any lifelong friends here?
Sure! I am still in touch with some of my classmates and professors.

What was your first job right out of College?
I went straight to graduate school in the States. And from school I went straight to the IMF.

What are your future goals? What more do you hope to achieve in the future?
I would like to stay involved in financial markets. I would also consider teaching economics and finance.

What career advice would you give a 22-year-old who is thinking about what to do with his or her life after College?
It's hard to tell in the abstract. It all depends on individual capabilities and aspirations. The general goal should be to figure out what fascinates you, what you love doing, and harness your talents to do it! ◆

Xafa at the International Monetary Fund headquarters in Washington D.C.