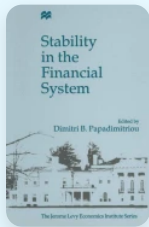


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# Finance and its Reform: Beyond Laissez-Faire

| Chapter


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## Stability in the Financial System

Gerard Caprio Jr. & Lawrence H. Summers


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## Abstract

The reform of financial systems is an area of economics which has seen broad swings in economic thought. For much of this century, with notable exceptions such as Schumpeter, orthodox thought was that money and finance did not matter or were not all that important in the development process. However, by the mid-1970s, the orthodoxy held that financial repression had to be stopped at all costs, and this liberalization in the financial sector led the way for the more general acceptance of the view that reliance on the free market should be complete. Likewise, in the early 1980s the pendulum swung back to the left in the approach

to financial systems a bit earlier than it did in other areas of economics. Based partially on evidence, especially from Latin America, that overly rapid reform had real costs, and partially on an increased appreciation of market failure in finance, it was accepted in the financial sector that blind adherence to free market principles was not quite appropriate.<sup>1</sup> And a counter-counter revolution is in sight, with some swing back towards the view that the market makes a mess of it but the government makes it even worse.

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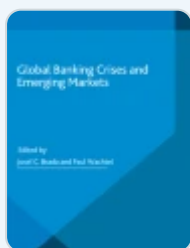
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